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COLLECTION OF FEDERAL FUEL TAXES

HEARING

BEFORE THE

SUBCOMMITTEE ON
ENERGY AND AGRICULTURAL TAXATION

OF THE

COMMITTEE ON FINANCE
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

SECOND SESSION

ON

S. 2075, S. 2003, S. 2062, S. 2067, S. 2118, and S. 2128

MARCH 16, 1988

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COLLECTION OF FEDERAL FUEL TAXES

WEDNESDAY, MARCH 16, 1988

U.S. SENATE,
SUBCOMMITTEE ON ENERGY AND
AGRICULTURAL TAXATION,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 9:50 a.m. in room SD-215, Dirksen Senate Office Building, Hon. David L. Boren (chairman) presiding.

Present: Senators Boren, Bentsen, Pryor, Daschle, and Wallop.

[The press release announcing the hearing follows:]

[Committee Press Release No. H-12]

SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION ANNOUNCES HEARING ON COLLECTION OF FEDERAL FUEL TAXES

WASHINGTON, DC—Senator David Boren (D. Oklahoma), Chairman, announced Monday that the Subcommittee on Energy and Agricultural Taxation will hold a hearing on recent changes in collection procedures on gasoline, diesel and special motor fuel taxes.

The hearing is scheduled for Friday, March 16, 1988, at 9:30 a.m. in Room SD-215 of the Dirksen Senate Office Building.

Boren said, "As a result of recent tax legislation, farmers, state and local governments and other exempt users must now bear the burden of certain diesel and gasoline excise taxes. Although these groups have no federal tax liability for their purchases of diesel or gasoline, they are now required to pay these taxes initially and apply for a refund later. This is clearly a situation which demands review."

[The prepared statements of Senators Boren and Pryor appear in the appendix.]

OPENING STATEMENT OF HON. DAVID L. BOREN, A U.S. SENATOR FROM THE STATE OF OKLAHOMA, CHAIRMAN OF THE SUBCOMMITTEE

Senator BOREN. We will commence at this point. We have several of our colleagues who are under tight time constraints. There are several other things going on at the same time this morning.

We are here to discuss the changes that were made under the Omnibus Reconciliation Act last year and the collection point of taxes on gasoline and diesel. They have also caused related problems affecting gasohol.

Chairman Bentsen of the full Committee on Finance has certainly indicated great interest in this matter. He understands the problem; and in fact with this hearing occurring today, Chairman Bentsen has taken the initiative to set a markup session on legislation that would correct this problem on Friday of this week.

So, expeditious action appears to be under way, and I know that that is something that is encouraging to all of us.

I am going to defer the remainder of my opening statement and place it in the record at this point; but needless to say these changes that have been made have put undue and harsh burdens both on local units of government, on State governments and on the agricultural community. This is a situation that cries out for change.

We already have too many burdens placed upon these segments already. They simply can't afford to shoulder them, and I am hopeful that the full Finance Committee and the full Senate and the House will act to correct this situation.

Let me turn to my colleagues and ask if they have any opening remarks that they would like to make. Senator Daschle?

OPENING STATEMENT OF HON. TOM DASCHLE, A U.S. SENATOR FROM THE STATE OF SOUTH DAKOTA

Senator DASCHLE. Mr. Chairman, I want to be very brief. We have a lot of our colleagues in front of us, but I couldn't agree more. This is really a vexing issue for a lot of farmers.

As I go out to South Dakota to talk about the broad range of issues affecting all of us, and getting into international policy and the broad range of issues that we are all affected by, the bottom line is: What are you going to do about the diesel tax?

And as we talk about diesel tax, if I had my way, we would deal with the heifer tax right away as well. Both issues—heifer and diesel—need to be addressed by this committee. I am pleased that the chairman has announced a markup for as early as Friday.

We have got to address this. We have got to uncomplicate the lives of these people, and we have got to do it as quickly as possible. We can't do it any sooner than Friday. Friday is soon enough, but the sooner the better.

Senator BOREN. Thank you very much. I am in full agreement with what you just said. I am also a cosponsor of the legislation on the heifer tax as well. Senator Wallop?

OPENING STATEMENT OF HON. MALCOLM WALLOP, A U.S. SENATOR FROM THE STATE OF WYOMING

Senator WALLOP. Mr. Chairman, let me add an echo to the heifer refrain. [Laughter.]

It is one of the more absurd things that we don't gather here for; that would turn ranchers into a bunch of lawyers.

From the moment of conception forward, you capitalize this critter, not knowing whether it is going to enter your herd or not. And I want to know who knows when the moment of conception is. The Supreme Court hasn't been able to determine that. [Laughter.]

But to the point at hand. I thank you for holding this hearing and scheduling the markup. This is an astonishing burden. That is one more reason why I am daily more delighted that I voted against the reconciliation package and the other tax bills that put it in place.

Just at a time when Wyoming ranchers and American ranchers are climbing a little bit out from under the worst period of econom-

ic despair they have had, here we go again and add as much as 27 percent to their up-front cost of fuel.

The same thing with the oil and gas industry, which does not need another blow and another economic burden to bear. I think in Wyoming there is over 9 million gallons of diesel fuel used in tax exempt use—and that is a major increase in cost at a time when there is a major decrease in profits, if any.

So, I think this hearing is just as timely as the action that this committee once took on a little old matter called withholding of dividends and interest. I think quite rightly the public rose up and told us what we had done. I think we might have been able to foresee what we had done in this instance, had we taken just a little more time on it, but I am glad we are here today.

[The prepared statement of Senator Wallop appears in the appendix.]

Senator BOREN. Thank you very much. Senator Pryor?

OPENING STATEMENT OF HON. DAVID PRYOR, A U.S. SENATOR FROM THE STATE OF ARKANSAS

Senator PRYOR. Mr. Chairman, I have a statement I would like to have placed in the record. I will not read that statement. I think today's hearing, Mr. Chairman, is indicative of this institution wanting very quickly to correct a wrong. We want to set the record straight.

We want to do what is right. This hearing was called, I think, on pretty short notice. In fact, Mr. Chairman, I am not even certain that I am a member of this subcommittee, but as of today, I am a member of it; I will guarantee you. [Laughter.]

Because of the amount of interest and the concern that we have heard from our farmers and from our people back home.

Senator BOREN. Since it sounds like you will vote right on this, I am sure we can arrange to make you a member of the subcommittee. [Laughter.]

Senator PRYOR. In Arkansas, we call this the Pryor/Daschle bill. I don't know what it is in South Dakota. [Laughter.]

But we want to do this, and we want to do it quickly and expeditiously. And I think the size of the hearing this morning, Mr. Chairman, is an indicator that we have got to do something and do it quickly. Thank you, Mr. Chairman.

Senator BOREN. Thank you very much, Senator Pryor. We will turn now to our panel of distinguished witnesses before us, and I will endeavor to see if any others have time problems. I know that Senator Exon is due to begin chairing another hearing just about now.

Senator EXON. Twenty minutes ago.

Senator BOREN. Twenty minutes ago, he says. So, we will begin with Senator Exon, if that is agreeable with the rest. We will go to Senator Domenici next, and Senator Gramm also has a problem. [Laughter.]

I see our friends from the other side of the Capitol noting this unusual senatorial behavior, but we are glad you are tolerant of it. We will begin with Senator Exon. We are glad to have you this morning.

STATEMENT OF HON. J. JAMES EXON, A U.S. SENATOR FROM THE STATE OF NEBRASKA

Senator EXON. Mr. Chairman, thank you very much. I ask that my complete statement be inserted in the record.

Senator BOREN. Without objection.

Senator EXON. So, let me be brief and summarize. First, I want to thank you for calling this hearing and having a markup on Friday. That shows that we can act around here when we have to.

In a nutshell, this act that we took in not recognizing the unfair burden that would be placed on our already overburdened farmers and ranchers in the United States is one that just cries out for immediate correction. The farmers and ranchers of the United States don't mind paying their fair share of taxes, but they certainly do not want or expect—nor is it fair—for them to be called upon to pay taxes that aren't even due.

And I think that is the crux of the situation. I recognize that the Finance Committee and the subcommittee thereof has a most difficult task, and you move promptly when you have to.

I thank you for your initiative here. I am proud to be a cosponsor of the Daschle bill, and I hope the Daschle bill or something very near to it can rapidly move through both the Senate and the House of Representatives, and I thank you for your consideration.

[The prepared statement of Senator Exon appears in the appendix.]

Senator BOREN. Thank you very much, Senator Exon. We will now hear from Senator Domenici.

STATEMENT OF HON. PETE DOMENICI, A U.S. SENATOR FROM THE STATE OF NEW MEXICO

Senator DOMENICI. Thank you very much, Mr. Chairman and members of the committee. I, too, will be very brief. I am sure before the morning is over, you will hear much more detail about this tax, but let me see if I can put it this way.

Clearly across this country we are concerned about the family farm. It, it is indeed ironic that we are asking American farmers to lend the Federal Government money for as long as possibly a year because they are sending taxes that they don't owe to be used by the American Treasury. They then must ask for a refund when they file their income taxes.

It seems to me we made a terrible mistake, and we just ought to undo it and undo it quickly. It is not a trivial matter because when you understand that on average this is between $400 and $425 per farm—it may be that for many it is much more, for some slightly less—but that is a lot of money when you are talking about a situation out there in farm country that we are all trying to help with and alleviate with all kinds of assistance, and the American people are urging that we help.

And here, we come along and do the exact opposite in this legislation. We ought to act quickly. We ought not assume farmers cheat. This is absolutely an inconsistent evaluation of how they conduct themselves. Frankly, I don't think we are going to collect any more money doing it the way we are than if we rely on the old-fashioned way of trusting them to claim their exemption up

front and not having to pay the Government and then get the money back later. Thank you very much.

[The prepared statement of Senator Domenici appears in the appendix.]

Senator BOREN. Thank you very much. I think the figure you pointed out shows that we are dealing with a very significant problem. We have so many farms under intense distress right now, barely hanging on; and to put this additional burden on them at this time is absolutely unfair. Senator Gramm?

STATEMENT OF HON. PHIL GRAMM, A U.S. SENATOR FROM THE STATE OF TEXAS

Senator GRAMM. Mr. Chairman, let me first thank you for holding the hearing, and I want to amplify what you said about a commitment in Congress to do something about this problem. We have had 17 bills introduced; we have over 218 cosponsors, if you bring all those bills together in the House; we have 52 cosponsors in the Senate.

The bill that I have introduced, S. 2003, I think probably has, more than any other, 35 cosponsors; but my recommendation would be that you bring all these bills together and that we cover everything.

Now, interestingly enough IRS has said we will take care of State and local government, but they have not taken any move to deal with farmers, ranchers, shrimpers, fishermen, oil and gas operators, and all the off-road users. I think it is imperative that we deal with all of them at once.

We have an opportunity, Mr. Chairman, to do something that Government seldom is able to do; and that is, since the tax does not go into effect until April 1, we have the remarkable opportunity to fix something before most people know it is broken.

And what a remarkable achievement that would be for Government to actually do that, and I would celebrate the opportunity to participate in it since it would be new and novel. Basically, our problem is in moving from collection at the retail level of the excise tax to collection at the wholesale level.

We have a situation now where exempt users—farmers, ranchers, oilmen, fishermen, shrimpers—are going to have to pay a tax they don't owe; they are going to have to keep records. If they pay in more than $1,000 in a quarter, they will be able to submit quarterly and get their money back. If they don't, they have to let the Government use their money for the full year.

Farmers would end up paying in about $426 million that the Treasury would have use of. You have similar figures, though smaller, for oil and gas people and fishermen, et cetera. I think this is an opportunity to act, to lift that burden from their shoulders; and I commend you for that effort and look forward to participating with you in the achievement of that goal.

Senator BOREN. Thank you very much. I think you are right; it would be unique if we indeed solved a problem of our own creation before it actually impacts the public. I think that might be a healthy trend that we could start around here.

As Senator Wallop has mentioned, the combination of this Act with the heifer tax—and we have not even mentioned yet because it is not under the jurisdiction of this committee, the crazy new regulation of the Federal Highway Administration on commercial operators, a license being required for people who might haul a five-gallon fuel tank or a little bit of fertilizer in the back of their pickups.

And we have a combined impact on a distressed sector that is almost unbelievable. I think you make a good point, too, about our attempting to get a comprehensive solution.

There are several approaches. We have the problem with both gasoline and diesel. We have some related gasohol problems, and we have other problems. So, it is my hope that the full committee will look at the provisions of all of the bills and attempt a comprehensive solution to it.

Now, we are very happy to have our colleague from the House with us this morning, Congressman Trent Lott. And I will just go down the list here now. Congressman Lott from Mississippi, we are very glad to have you with us this morning.

STATEMENT OF HON. TRENT LOTT, U.S. REPRESENTATIVE FROM THE STATE OF MISSISSIPPI

Congressman LOTT. Thank you, Mr. Chairman. I appreciate this opportunity to appear with this very distinguished panel. I want to ask consent that my prepared statement be made a part of the record.

Senator BOREN. We will be glad to do that.

Congressman LOTT. I would also like to commend this subcommittee—you, Mr. Chairman—and the full committee and all my colleagues from the House and the Senate who have really gone to work on this very important matter expeditiously.

I especially want to commend this committee for having the hearing and hopefully acting on it on Friday. I think that will give us a little more incentive in the House to get going. We do have bills, similar bills to your bills here in the Senate, that we have introduced in the House.

I have already discussed this matter with the Secretary of the Treasury, Jim Baker, and he made it very clear that we were going to have to act on this legislatively. They couldn't remedy the problem administratively.

I have had the opportunity to talk to the Chairman of the Ways and Means Committee and also our ranking member John Duncan; and they assure me they are going to move quickly; but this April 1 deadline is a serious problem for us. So, we really do need to get moving.

I would like to point out, as Senator Wallop mentioned in his remarks, that this is similar to what has happened a couple of times in the past. You mentioned the withholding of the interest and dividends—the tax on interest and dividends. Also, I think another similarity was the logging of mileage of automobiles and trucks for farmers. Remember?

We came back very quickly and remedied that problem. And I do think that this time, if we could do this before April 1, it would be very significant.

I would like to also emphasize, as Phil was just touching on, that while this is very important to a lot of segments, I know it is very important to farmers; and I have heard from an awful lot of farm and farm-related organizations in the State of Mississippi.

It also affects fishermen and shrimpers; and a lot of times when you have a single shrimp boat operator, this is the margin of profit that he—and she sometimes, if his wife is working with the shrimper—they just won't be able to make it with this additional burden.

Following now on the heels of having to deal with the so-called "turtle excluder device" that Congress put on them last year, this is just going to be the straw that breaks their back.

Also, I want to mention that it affects the tow boat operators, the barge operators. We shouldn't forget that it affects farmers and a lot of the fishermen, and also the river boat operators. So, I do think that it is very important that we put everybody in here who would be adversely affected and not have to do it piecemeal, and then we can all be together as we go forward.

I think those are really the main points I wanted to make. This was an oversight; we do need to correct it. Thank you for your effort, and I want to commend you. These are the shortest remarks that I have ever heard by Senators under any circumstances. [Laughter.]

I am very impressed with the way your colleagues here in the Senate are moving on this issue. Thank you, Mr. Chairman.

Senator BOREN. Thank you very much, Congressman Lott. We are very appreciative of your joining us, and we wish you well in your efforts on the other side of the Capitol, as we move ahead here.

I want to turn now to my colleague from Oklahoma and thank him for his patience, as I have called upon others. Senator Nickles was one of the first members of the Senate to introduce legislation to correct this problem. He was one of the first voices raised in protest against this action, and we are very glad to have you with us this morning.

[The prepared statement of Congressman Lott appears in the appendix.]

STATEMENT OF HON. DON NICKLES, A U.S. SENATOR FROM THE STATE OF OKLAHOMA

Senator NICKLES. Mr. Chairman, thank you very much. I likewise will echo the compliment. I appreciate the subcommittee having the hearing today and I am pleased that the full committee will be marking up this Friday.

I think it is awfully important that we do move as quickly as possible, and I would echo the comments of Senator Gramm. I think it would be wise to package as much as possible. We have several bills that are pending, that have been introduced.

I have one or two; Senator Dixon and I will introduce a more comprehensive bill. Senator Daschle, a lot of your work as well is to be complimented.

I would just hope that we can put together a bipartisan package that can move very quickly through Congress. We have heard several comments; and most of the comments have been made concerning the diesel changes that need to be made for farmers, for ranchers, for oil operators, for commercial fishermen.

I hope and expect that we will be successful in moving and making some changes. We have heard the figure dealing with farmers; an average farmer would pay $400.00. We checked the average wheat growers in the State of Oklahoma. The average diesel fuel excise tax would be $900.00 for them.

This means that those farmers would be paying these taxes, keeping track or trying to keep track—and that is easier said than done—of all the receipts. Eventually, they would file for return; they would have to wait.

So, they would be making a no-interest loan to the Federal Government, keeping all the paperwork burden, filing for the return, and eventually hoping to receive a return.

We don't need to put an administrative burden nor should we be mandating the farmers and ranchers and oil operators and others be making no-interest loans to the Federal Government.

So, we need to act and act now, and I compliment you.

I haven't heard much today dealing with State and local governments. I heard Senator Gramm say that we could move quickly and solve this problem before it goes into effect. If we did, that would deal with the diesel tax and that would be good; and I hope that happens.

Unfortunately, the gasoline tax, as far as State and municipalities, has already gone into effect. You have cases where these groups, which have never been forced to pay the tax before, beginning January 1 of this year have had to pay the tax.

So, now you have cities and counties and States and universities that have to pay the tax. And you talk about a paperwork nightmare; I am thinking of my home town in Ponca City, Oklahoma. They would end up paying taxes of about $13,000 in the course of the year. That means keep records for the fire department, the police department, the municipal employees—all these various agencies.

They would collect the data. If they cross a certain threshold, they can file for a refund and maybe they could get it quarterly; but in all likelihood, they would do it annually. So, it would be making a no-interest loan.

No telling how much money they would have to pay for clerical help to keep track of all these records.

The State of Oklahoma is a much larger figure, $771,000. The city of Tulsa would pay $158,000—they would be loaning to the Federal Government, receiving no interest whatsoever. That makes no sense.

And again, the administrative or clerical costs are enormous, not only on the cities but on the Federal Government because they are going to have to audit these. Before they start writing refund

checks, they are going to try to make sure that those figures are accurate.

Again, this became effective January 1; and so, there is enormous support for repeal of these provisions, to allow these nontaxable municipalities and governmental units to maintain their previous status and not have to file for the refund.

You will hear from other witnesses today who will testify to the fact that we have had a large number of cosponsors on the bill that I have introduced. I hope and expect that many would include this in an overall comprehensive package, and I thank you for your efforts.

Senator BOREN. Thank you very much. I think you make a good point about the gasoline problem. We do have a approximately 83,000 units of government, it is estimated in the country that are impacted, creating a nightmare in terms of keeping records and lost revenue

We also have in addition—and I don't believe this has been mentioned yet this morning—the problem that gasohol blenders also have. It has a great impact on them as well.

Senator NICKLES. Correct.

Senator BOREN. So, we do have a problem that calls out for a comprehensive solution, as you have indicated.

Senator NICKLES. Mr. Chairman, just to follow up on that, the legislation that Senator Dixon and I will introduce today deals with the gasohol problem; and also, to clarify, we have heard that cities were taken care of. That was an exemption dealing with the diesel, which requires a lot of bureaucratic response, and most of the cities say it is not really workable and does not solve the problem with their having to prepay the gasoline tax.

Senator BOREN. The gasoline tax. Right.

Senator NICKLES. And that is the biggest bulk of the money.

Senator BOREN. Right.

Senator NICKLES. That is a very important point.

Senator BOREN. Again, I congratulate you on your leadership on this matter.

Senator NICKLES. Thank you.

[The prepared statement of Senator Nickles appears in the appendix.]

Senator BOREN. And we are glad to have our colleague from the House, also from Nebraska, Congressman Hal Daub, with us this morning. We appreciate your patience as others have been testifying.

We are very glad to have you this morning and appreciate your activities in this area of tax policy as well. We will be happy to hear from you at this time.

STATEMENT OF HON. HAL DAUB, U.S. REPRESENTATIVE FROM THE STATE OF NEBRASKA

Congressman DAUB. Mr. Chairman, I am delighted to be here today, and I want to salute you and your colleagues for expediting this matter. I think it is an important subject for consideration.

Just as the automobile and vehicle mileage record keeping idea was well intended—you know, that Rolls Royce that was over in

the country club parking lot at 10:00 in the morning on Sunday for brunch—it never showed up in the company parking lot, and it was being written off. The regulations went too far, but by exception, we had to correct it legislatively.

The same thing here. With good intention, with respect to compliance, we allowed airplanes and railroads and certain municipalities and certain other stationary diesel use to be exempt by not specifically legislating all the other exemptions; we end up now having to cure this legislatively.

We agreed that we don't want the Commissioner of Internal Revenue Service to be picking and choosing which laws he enforces and which ones he doesn't. So, your leadership today and the early markup that you have scheduled, Mr. Chairman, I think are to be commended; and I am hoping for the same opportunity in the House.

The Daschle bill is a good one. Congressman Dorgan, my colleague, and I have offered a bill, H.R. 3844, in the House. We are members of the Ways and Means Committee. It has an earliest date of January 25th; it has an 85 to 90 cosponsorship, as Phil Gramm said, and over half the House have now sponsored a variety of good pieces of legislation; and we are looking for expedited bipartisanship on this matter as well.

We talked to Commissioner Gibbs several times. The good news and bad news was that we got a three-month extension on the ethanol regulation publication to give us a little breather there, but all the other things are going to have to be dealt with legislatively.

I want to particularly stress the plight of the farmer. A farmer who has to file his income tax return by the first of March does not have a W-4 against which he could claim a larger number of exemptions, thereby lowering some tax from another anticipated increase, or file a quarterly estimate, as most others in business do, thereby having some flexibility to lower their estimated tax in anticipation of higher gas taxes, for example.

The farmer doesn't have that flexibility, and few will purchase $8,000 or $10,000 worth of diesel or gasoline to be able to pay an extra $1,000 worth of tax to claim the quarterly refund. So, they will have to set off in most cases, their collection or their refund for at least a year, plus the processing time, and probably include in the planting operating loan and/or the harvesting operating loan the additional cost at interest to the producer/grower without the refund similarly paying that borrower back the interest that the Government will have avoided by using the taxpayer's money.

It is a tax that is not owed. It should, therefore, not be collected because the collection, in the interim, should not be used to fund the central Government's expenses for food stamps or foreign aid. That is not what a tax is supposed to be used for if, by any other name, this is in fact not a tax.

So, I would hope that, because of the particular and unusual circumstances of those in agriculture, this cries out for an extraordinary remedy, along with those similarly situated in shrimping and trucking and construction who have stationary, off-road use and particularly municipalities, those below the State level, who would otherwise be given an in-lieu-of tax treatment as they always have been under our Tax Code.

The bill we authored, Congressman Dorgan and I, offers several other ideas that I would urge you to consider. One is the Pickle Amendment which would allow registered wholesale dealers to purchase gasoline without paying the tax to the refinery or terminal if they are bonded or supply proof of financial responsibility.

Finally, we address the alcohol/gasohol/ethanol blended fuel issue, and we are concerned as well about the timing problems that would essentially cause blenders simply to give up offering that very important market for agricultural grain.

I really do appreciate the opportunity to testify. I thank the Senate committee for their attention and their courtesy.

Senator BOREN. Thank you very much. You have certainly outlined the many ways—the diesel tax collection process impacts on the farmer.

I believe Congressman Lott mentioned the impact on inland waterways. We see this, for example, in the Port of Catoosa in our State where, again, much of the product that is moving is bulk agricultural product. So, we have an additional add-on to the cost of transportation, as well as to the cost of production, which is a very large total impact.

Congressman DAUB. Senator, I might add one final point, and that is that we are commencing to distort the petroleum marketing pipeline.

Senator BOREN. Yes.

Congressman DAUB. Out in my part of the country—and I don't know any of yours, gentlemen—but in fact, people are trying to put as much as they can in every tin cup and bucket they can find. [Laughter.]

The result of that is going to be a distortion of pipeline and supply and price. In some cases, I am told, diesel has gone up as much as a dime a gallon in the last 2 weeks. Now, that is just not fair.

Then, of course, for our refiners and wholesalers, three months after this April 1 deadline it is also going to create a serious problem. So, it is a situation that really does cry out for prompt action, and we have proven before that we can do it; and I hope that Congress does it again.

Senator BOREN. Thank you very much.

[The prepared statement of Congressman Daub appears in the appendix.]

Senator BOREN. Senator Wallop?

Senator WALLOP. Let me just make an observation. Make no mistake about it, this was done on purpose to force this loan. The idea was not efficiency in the point of collection but, in fact, to have a cash flow to the Federal Government. This is one of the reasons why this trend should be stopped. We should stop it right here and right now and make clear to the American people that what we are not going to do is force them to subsidize the Federal Government in a manner we are unwilling to levy. We somehow or another have just found another way of raising revenues.

So, this was a revenue-raising procedure. It was a revenue-raising procedure disguised as more efficient collection to get rid of waste, fraud, and abuse. In point of fact, it really was a directed

means by which we would have a cash flow circumstance that was favorable to the Federal Government and not to the taxpayer.

Congressman DAUB. May I make one other comment in response to Senator Wallop? That is, indeed that is true. It is a revenue issue, in a way, but it is not a compliance problem to the extent that it was perceived; and if you look at the House and the Senate record, the actual process has been abused because neither the original Senate bill nor the original House bill contained this intention.

So, in conference, with the press of business in December, some well-intended exceptions were made; but it wasn't as thoroughly considered as it ought to have been. We now can give that opportunity for process to shine in.

As Senator Gramm said a week ago in the House committee in testimony, the crime of all this would be that, once we find this difficulty, we fail to correct it.

Senator BOREN. Thank you very much. Senator Murkowski, I know, has a scheduling problem this morning. We are very glad that you have joined us, and we will hear from you at this time.

STATEMENT OF HON. FRANK MURKOWSKI, A U.S. SENATOR FROM THE STATE OF ALASKA

Senator MURKOWSKI. Thank you very much, Mr. Chairman. I appreciate the opportunity to give you the point of view from the fishermen and, as you may have observed in your travels up and down at least the West Coast, there are not an awful lot of fishermen that use the highways; and they are a little befuddled by the bookkeeping that the Federal Government has proposed.

I think the Senator from Wyoming was quite right when he suggested that this is a very dangerous process, and the idea of using somebody's money for a period of time to make figures look better on various reports is just what the Federal Government is up to. They are taking the taxpayer's money in advance and then, when they are going to have to pay the taxpayer back through a refund they do it through a process known as adding to the deficit or the accumulated debt ultimately. And those kind of bookkeeping transactions should be not just curtailed, but exposed for what they are.

Let me tell you first of all, Mr. Chairman, that I am here today joining my colleague from Virginia, Senator Warner, and others on S. 2128 to permit tax-free sales of diesel fuel for off-road use by commercial fisheries and vessels specifically, as well as, of course, the inclusion of other traditional off-highway use—agriculture and others.

And the idea of this Mickey Mouse formula of collecting and then paying it back, as I have indicated previously, should be curtailed immediately.

Let me make a few points, and I would like my entire statement entered into the record, as if read, Mr. Chairman.

For example, these new tax collection changes are going to cause tremendous cash-flow problems for diesel fuel wholesalers that sell on credit; and this is a large segment of the smaller wholesalers that are in existence. Wholesale fuel dealers are going to have to sell continued on the basis of the relationship they have with their

customers, particularly fishing vessels, on 30 to 90 day credit terms because, obviously, the fisherman only gets paid when he sells his catch.

The new changes require that wholesalers collect and pay the diesel fuel taxes to the IRS within one to three weeks of the sale. As a result, the wholesalers are going to end up paying thousands and thousands of dollars of their customers' fuel taxes before they are paid by their customers.

That is the way the credit system works, and it works all over the country in that regard. It is estimated that a typical wholesale fuel dealer in Kodiak Alaska—one of the major fishing ports—who sells perhaps a half million gallons of diesel fuel per month is going to have to pay $75,000 in new up-front, out-of-pocket tax payments. He is probably going to have to go to the bank and borrow it.

It would cost the fuel dealer in Dutch Harbor—an isolated area out in the Aleutian Islands—even more perhaps as much as $450,000 a month.

So, I think it is fair to say, Mr. Chairman, that under the new tax law, the sales are permitted where diesel fuel is sold for use as heating oil; they don't have to pay it in that area; and in cases where the IRS determines that the diesel fuel is destined for a non-taxable off-highway use.

Fuels sold for use in diesel-powered trains, commercial aircraft, industrial plants, and to Government entities may be sold tax-free. I think this should be extended at the very least to the fisheries industry and the fishing vessels.

I see my time is up, and I want to thank you for the opportunity to present this testimony on behalf of a good segment of American industry that is having a tough time out there competing and throw on more regulations and more reporting on them isn't going to help them compete in the markets of the world. Thank you, Mr. Chairman.

Senator BOREN. Thank you very much, Senator Murkowski. We appreciate your comments and we will enter your full statement into the record. We have been joined by our colleague, Senator Karnes of Nebraska, whom I have been privileged to serve with on the Agriculture Committee; and we have worked together there on a number of important farm issues, and we would be happy to hear from you at this time.

[The prepared statement of Senator Murkowski appears in the appendix.]

STATEMENT OF HON. DAVID K. KARNES, A U.S. SENATOR FROM THE STATE OF NEBRASKA

Senator KARNES. Thank you, Mr. Chairman. It is a pleasure for me to be here, and I appreciate the expeditious fashion in which this committee called itself to order in order to deal with this very important issue.

Mr. Chairman, I would rather not be here today because this whole episode, in my mind, symbolizes how poorly Washington handles its business. The diesel fuel tax ranks up there in my mind

with the $700 toilet seats as one of the most stupid things that I think has ever occurred around here.

Frankly, none of us should have to be here at all because this tax that we want repealed should never have been enacted in the first place. As you know, beginning April 1 farmers all across this country are going to have to pay a 15 cent Federal tax on each gallon of diesel fuel that they buy, and they will have to file for a refund because the Government owes the farmers what they have paid.

I would like for someone around—anyone—to explain to me the logic and fairness behind this bizarre process. This is a classic Federal revenue shell game using the American farmer's hard-earned money.

The legislative history of this tax is as murky a the tax itself. I have looked for and cannot find any reports on hearings; the tax just appeared like magic. I am told that it was the House Ways and Means Committee where this tax first sprouted; and because it was in the massive 43 pound reconciliation measure, it was like a needle in a haystack—invisible to all except those who knew it was there.

And those who knew it was there wanted it there because it was the purest, blue smoke in mirrors way to raise more revenue. I must surmise that the Ways and Means Committee drafters were counting on the majority of farmers would not comply with the refund procedures of the tax and that the Federal Government would then be the beneficiary of this ill-devised windfall.

Mr. Chairman, the USDA estimates that this tax shuffle will cost farmers more than $460 million annually. In order to pay these costs farmers will be forced to borrow additional operating capital and, of course, be charged interest for whatever they have to borrow.

In addition, farmers will face a horrendous paperwork task as they try to keep track of farm use and all their diesel fuel vehicles. I am a fourth-generation Nebraska farmer who still owns and operates a family farm in south central Nebraska. I estimate that the family that currently operates our farm will have to spend an additional $1,700 on fuel costs in the coming year. That is an increase of approximately 20 percent in their current outlays for diesel fuel. Over the past year, approximately 11,250 gallons of diesel fuel was used on our farm, at an average cost per gallon of 67 cents.

Another 15 cents per gallon would raise the cost of that fuel to 83 cents a gallon. Our farm is an average size feed grain operation. Many farmers, of course, with larger operations will face even greater costs associated with this provision.

As a member of the Senate Agricultural Committee, I have been closely watching the recovery that has begun across rural America. In the last several months, I have held more than 30 town hall meetings throughout Nebraska, and the diesel fuel tax—or more accurately, the stupidity of it all—is topic number one.

I have even had farmers and ranchers in Nebraska tell me that, if we want to tax diesel fuel, let's do it; but do it honestly by holding hearings and then voting for this tax as a stand-alone measure. Just don't try to pull the wool over anyone's eyes because they are not fooling a single person, particularly in Nebraska.

I doubt, Mr. Chairman, that if we were allowed to vote on a diesel fuel tax in the above-the-board fashion that we would probably pass it. The economic recovery in rural America is tenuous and does not extend to all parts of our country.

While we are spending billions of dollars to help our farmers recover, we should not be imposing new costs or even more costly, frustrating paperwork burdens on them.

And they certainly should not have to waste so much as one minute jumping through these needless tax hoops.

Mr. Chairman, I am a cosponsor of Senate bill 2003, the first bill introduced in the Senate which seeks to repeal this tax and to refund the amount paid by farmers during the tax period that was collected. I urge my fellow colleagues in the Senate to join me in adopting this measure, which is entirely consistent with logic and fairness for our American farmers.

The diesel fuel tax should be repealed and it should be repealed now before spring planting begins in earnest in only a few short weeks. Thank you, Mr. Chairman, again for the opportunity to testify.

Senator BOREN. Thank you very much, Senator Karnes.

I will enter into the record a statement by Senator J. Bennett Johnston, who had planned to be with us this morning, and also by Senator John Warner of Virginia.

[The prepared statements of Senators Johnston and Warner appear in the appendix.]

Senator BOREN. And let me say, in talking about the plight of the farmer and the fact that many of the farmers have not yet experienced the recovery that is often talked about, that is certainly the case in my State. As I said, many of these farmers are just barely hanging onto the family farm; and when we do have these town meetings and when we do get together with our farmers—especially when they consider things like the diesel tax, the heifer tax, and some of the other things that are being done—they turn to us and they say: Do you really care? Does anyone up there really care about the problems that we are having, hanging onto the family farm?

And that is what we hope to demonstrate; we do care, and we hope to demonstrate that by expeditious action to take care of this problem.

Let me say we have just been joined by the chairman of the full committee. Beginning with my first discussion with him about this problem, he has been right on top of it. He is intent, I know, on expeditious handling. He has already scheduled a markup, and no one has been more ready to consider the problem than my good friend, Senator Bentsen from Texas.

I would like to call upon him now for any comments that he might like to make.

Senator WALLOP. Mr. Chairman, before we proceed, can we affirm that this is a half-hour vote?

Senator BOREN. This is a half-hour vote. I will explain to our guests that that is the reason that some of the committee members have been leaving. We will take turns and try not to disrupt the proceedings; but we do have a roll call vote in progress. Chairman Bentsen?

OPENING STATEMENT OF HON. LLOYD BENTSEN, A U.S. SENATOR FROM THE STATE OF TEXAS, CHAIRMAN, SENATE FINANCE COMMITTEE

Senator BENTSEN. Thank you very much. I want to thank the distinguished Senator from Oklahoma for holding these hearings. I think they will be very helpful to us.

The diesel tax change in the 1987 Reconciliation Act was first proposed by the Administration last year. At that time, the head of the Federal Highway Administration came in to tell me that there was about $500 million per year in diesel tax evasion. He proposed moving the collection point of diesel taxes to the wholesale level.

The Administration also recommended moving the collection point in budget deliberations last fall with the House and to the Senate. The House passed the provision first, and then it was brought to us.

I then received a call from a 94-year-old farmer down in south Texas who told me that he really thought it was a most unfair deal. He said: You know, farmers in Texas are in real trouble and are short of capital. And here, you have a situation where the Government is going to take a free ride on them. The Government is going to collect a tax from farmers that they don't owe. It just doesn't make sense to do this, especially at a time when farmers have a shortage of capital, profits are down, and farm foreclosures are occurring at very high rate.

And I said: Well, Dad, you are making a good point. [Laughter.]

And I said: But you have this situation where there is $500 million per year in diesel tax evasion. Well, obviously, we now know the provision was not fair. And now, we have heard from the various groups that are affected by it—farmers, oil drillers, and other off-road users. Today, we are looking for different proposals to take care of tax evasion, get rid of it so that the Government collects what it is entitled to.

But the Government should not get a free ride on farmers who are already in trouble. We are seeking alternatives to accomplish that goal. That is why we have asked Treasury and the Highway Administration to appear as witnesses today—to give us some alternative options.

That is also why I have asked good friends of mine like S.M. True, who heads up the Texas Farm Bureau, who has heard from all of his membership concerning this, to testify today. I am delighted he is here this morning.

As most of you may know, I have called for a markup on Friday. We are going to address this diesel tax issue at that time. I can tell you that we are going to correct it. We are going to try to put the diesel tax collection procedure back on an equitable ground so that we can achieve the objective of stopping tax evasion, without putting an undue burden on farmers and oil producers.

Senator Boren, I am just delighted that you are having this very timely hearing. We will address some of the issues that you bring forth today in our markup Friday, and try to take care of this problem.

Then, I am going to make a call to a 94-year-old farmer down in south Texas and get some credits with him. [Laughter.]

Senator BOREN. Thank you very much, Senator Bentsen. Sometimes we have the frustration around here of not being able to get committees to act and not being able to get markup sessions called; and let me say it is a breath of fresh air to be able to work with Senator Bentsen and to see his intention of moving very quickly on this. And that is very much appreciated by all of us on the committee.

I am going to call now—and I might ask both to come forward—Mr. Dennis Ross, the Deputy Assistant Secretary for Tax Policy, representing the Department of the Treasury; and also Mr. Robert Farris, the Administrator Designate of the Federal Highway Administration.

We will begin at this time by hearing from Mr. Ross on behalf of the Treasury Department.

STATEMENT OF HON. DENNIS ROSS, DEPUTY ASSISTANT SECRETARY FOR TAX POLICY, DEPARTMENT OF THE TREASURY, WASHINGTON, DC

Secretary Ross. Thank you, Mr. Chairman. I am pleased for the opportunity to present the views of the Treasury Department regarding possible changes in the collection procedures for the Federal excise taxes on gasoline and diesel and aviation fuel.

As you know, Mr. Chairman, recent legislation has shifted the point at which these taxes are collected to a higher level in the distribution chain—from the wholesale to the bulk storage terminal level in the case of gasoline, and from the retail to the wholesale level in the case of diesel and aviation fuels.

In each case, the change was made in order to address serious tax evasion problems by reducing the number of taxpayers permitted to make purchases on a tax-free basis. We believe these changes, which mirror changes that a number of State governments have made to improve collection of their own fuel excise taxes, will prove highly successful in addressing evasion of Federal excise taxes.

We do recognize, however, that the changes have raised collateral problems for consumers that use fuel for tax-exempt purposes. I will, in the course of my testimony, discuss some of those problems.

I will first today describe the collection procedures for the fuel excise taxes and the treatment under those procedures of tax-exempt purchasers. Next, I will describe recent proposals that would revise these collection procedures and indicate the Treasury Department's views regarding those possible revisions.

Turning first, Mr. Chairman, to the gasoline excise tax, as you know, that tax is a substantial revenue source, raising approximately $9.1 billion in fiscal year 1987. The tax rate is 9.1 cents per gallon of gasoline with 9 cents per gallon dedicated to the Highway Trust Fund and the remaining .1 cent per gallon transferred to the Leaking Underground Storage Tank Trust Fund.

Certain uses of gasoline are fully exempt from the tax, including export uses, use by State and local governments, and use on a farm for farming purposes. Other uses are partially exempt from the tax, including use in gasohol, which is taxed at the reduced rate of 3.1 cents per gallon.

Prior to January 1, 1988, the gasoline excise tax generally was imposed on the wholesale dealer at the time gasoline was sold to a retail dealer or, in some cases, to the ultimate consumer.

Wholesalers and other persons above the retail dealer level were entitled to purchase gasoline on a tax-free basis, provided they were registered with the Internal Revenue Service.

Under this prior system, approximately 12,000 tax-free purchasers were registered with the IRS. Evasion of tax under the prior system was widespread, amounting by our estimates to approximately $250 million per year.

Evidence further indicated that organized crime and others were involved in evasion schemes, generally involving persons registered as wholesale dealers selling gasoline at a price that included the excise tax, but then failing to remit that tax to the Federal Government.

In an attempt to prevent or at least minimize such evasion, the Tax Reform Act of 1986 shifted the collection point for the tax upstream to the point of removal or sale of gasoline by the refiner, importer, or terminal operator.

Since the amended statute permits bulk transfers of gasoline to registered terminal operators without payment of tax, tax in general under these revised rules is imposed at the point the gasoline leaves the bulk storage terminal.

These changes in the collection system, as you know, were effective on January 1, 1988.

Turning to the diesel and aviation fuel excise taxes, the tax rate on diesel fuel is 15.1 cents per gallon; the rate on aviation fuel, 14.1 cents per gallon. Of these amounts, 15 cents per gallon of the diesel tax is transferred to the Highway Trust Fund, and 14 cents per gallon of the aviation fuel tax is transferred to the Airport and Airway Trust Fund.

The remaining .1 cent per gallon, in the case of each tax, is transferred to the LUST Trust Fund. As with the gasoline excise tax, certain uses of diesel and aviation fuel are exempt from tax, again including export, use by State and local governments, and use on a farm for farming purposes.

In fiscal year 1987, excise tax receipts from the diesel and aviation fuel taxes were $2.7 billion and $.1 billion respectively.

As you know, under the 1987 Budget Reconciliation Act, the collection procedures currently in effect for the diesel and aviation fuel taxes will be changed, effective April 1 of this year. The current procedures impose the tax on the sale to the ultimate consumer, that is, generally at the retail level.

By maximizing the number of persons involved in collecting tax, the current procedures have encouraged development of tax avoidance schemes. And similar to the changes adopted for the gasoline tax, the 1987 Act attempted to improve compliance by shifting the point of collection upstream, from the retail to the wholesale level.

Under these new procedures, the tax will generally be imposed on the wholesale dealer at the time the fuel is sold to a retail dealer, or again, in some cases, to the ultimate consumer.

Mr. Chairman, let me now discuss the reasons for these changes in collection procedures with respect to the diesel and gasoline taxes.

Movement of the collection point has a number of positive compliance effects. First, it results in a shorter audit trail by reducing the number of times that fuel changes hands between the time the fuel is produced and the time the tax is imposed.

Second, it reduces the number of transactions on which the tax is imposed, while increasing the average volume of fuel per transaction.

Third, it reduces the number of persons that are eligible to purchase fuel tax-free and then remit the tax to the Federal Government. In case of the gasoline excise tax, the move upstream in collection point reduces the number of persons remitting the tax to the Government from approximately 8,000 to an estimated 1,000.

In the case of the diesel tax, the upstream movement in the collection point will reduce the number of persons remitting the tax from approximately 60,000 to an estimated 8,000.

And finally, taxpayers at the higher level in the distribution chain can be expected on average to be financially sounder and to maintain better records of their transactions than persons at a lower level in the distribution chain.

As a consequence of these positive compliance effects, we believe there will be dramatic reductions in the amount of revenue lost through excise tax evasion. In particular, we estimate that the 1986 Act changes will increase gasoline tax revenues by approximately $300 million in fiscal year 1988 and approximately $200 million per year in fiscal years 1989 through 1993.

Part of that initial revenue effect, I should note, is not due to improved compliance, but to an acceleration of tax collections.

In the case of the diesel and aviation fuel taxes, the 1987 Act changes will increase revenues by approximately $350 million in 1988, $250 million in fiscal year 1989, and $200 million per year thereafter. Again, the initial revenue figures reflect in part an acceleration, and not simply an improvement in compliance.

Senator DASCHLE. If you could summarize your testimony, Mr. Ross?

Secretary ROSS. Mr. Chairman, I will do my best to do that.

Senator DASCHLE. We have a 5-minute rule, and we would appreciate it if you could summarize.

Secretary ROSS. Is that applicable?

Senator DASCHLE. Yes.

Secretary ROSS. All right. I have probably used my 5 minutes.

Senator DASCHLE. The red light is the indication when your time has expired, but for you, you are worth at least a couple more minutes.

Secretary ROSS. All right. [Laughter.]

Senator DASCHLE. So, by all means, give us as succinct a summary as you can, but by all means, give us whatever testimony additionally you would like to pursue.

Secretary ROSS. All right. Mr. Chairman, let me turn, directly to the proposals that have been made to revise the current collection procedures.

Since the 1986 Act was passed, as you know, proposals have been made that would—with respect to the gasoline tax—partially reverse the changes made in the 1986 Act. In particular, S. 2067

would permit gasoline wholesalers to buy gasoline on a tax-free basis and then remit the tax to the Federal Government.

We oppose S. 2067 since we believe it would substantially increase the number of persons permitted to buy gasoline on a tax-free basis and thus increase the very opportunities for evasion that Congress intended to prevent in the 1986 Act.

We have previously estimated that changes of the sort contemplated in S. 2067 would lose $30 million in revenue in fiscal year 1988 and $60 million each year thereafter.

In addition to proposals such as S. 2067 that would again change the point of collection there have also been proposals made to provide an up-front exemption from the tax for gasoline destined for use by State and local governments or by farmers.

S. 2062 and S. 2067 are examples of such proposals.

We have serious reservations about these proposals because we believe they also would create opportunities for tax evasion that the 1986 Act intended to close. This is particularly true of any approach that would exempt from tax all sales of gasoline certified by the purchaser to be destined for nontaxable use.

Turning quickly to the proposals affecting diesel fuel excise tax collection procedures, numerous bills, as you know, have been introduced that would add farmers to the categories of exempt persons permitted to make tax-free purchases of diesel fuel. Some proposals, such as S. 2075—your own proposal—would authorize Treasury to permit farmers to make tax-free purchases on the same terms as the categories of purchasers currently permitted to make such tax-free purchases.

Other proposals, such as S. 2067, would permit farmers to make tax-free purchases at the retail as well as at the wholesale level.

Mr. Chairman, the Administration has under review your own proposal, S. 2075, that would extend regulatory authority to permit tax-free purchases by farmers at the wholesale level. Because of the potential for evasion, however, we would not support permitting farmers or other exempt users to make tax-free purchases at the retail level as proposed by S. 2067 and certain other proposals.

Moreover, we believe that the privilege of making tax-free purchases should be subject—however it is expanded—to such regulatory or registration requirements as the Treasury Department may determine are appropriate.

We estimate that the revenue loss from permitting tax free purchases of diesel fuel for farm use at the wholesale level is $120 million in fiscal year 1988, $75 million in fiscal year 1989, and $20 million per year thereafter.

Extension of the right to make tax-free purchases to additional groups of exempt users would adversely affect compliance and hence further reduce the revenue gains that were anticipated in the 1987 Act. Thus, we estimate that amending the 1987 Act provisions to permit all groups purchasing for exempt uses to make tax-free purchases at the wholesale level—even though such groups would be subject to appropriate registration requirements—would result in revenue losses of at least $80 million per year on an ongoing basis.

Finally, Mr. Chairman, though I need not summarize it here, my testimony notes some alternative approaches to alleviating the

burden on tax exempt purchasers of diesel and gasoline fuels—alternatives, that is, that would focus perhaps on expedited refund procedures or on extending the provision that exists under current section 6416 of the Code, which in appropriate circumstances can allow a tax-exempt purchaser to make the initial purchase free of tax, and effectively assign the refund right to a person higher up in the distribution chain.

That concludes my prepared remarks. I stand ready to answer any questions.

Senator BOREN. Thank you very much, Mr. Ross. I think we might pause for questions here that might be directed to you. Senator Daschle?

Senator DASCHLE. Thank you, Mr. Chairman. I would ask Mr. Ross: In the case of farmers it seems to me that they have a problem unique to agriculture compared to other off-road users. They don't file the quarterly reports; and as a result, they can't claim a refund on their quarterly estimated returns.

How do you propose we address that problem?

Secretary ROSS. I think you are right, Senator Daschle. That is a problem, peculiar in a sense to farmers. They don't generally pay estimated taxes, and thus don't have that offset ability that other exempt users might well have. And I think that makes the case of farmers perhaps especially sympathetic.

As I said, we have under review your own proposal that would take account of that and allow farmers, on the same basis as some other groups, to make tax-free purchases at the wholesale level.

Senator DASCHLE. Mr. Ross, the bill has been introduced now for some time and you have heard our Congressional witnesses. We have had a number of bills introduced. We are bumping up against the deadline, soon to be here.

You say the bill is under review. Can't you be more definitive than that today? Can you give us a little more enlightenment with regard to your position, especially relating to farmers?

Secretary ROSS. Let me try. The bill is under active review at the White House; and for that reason, I cannot speak authoritatively as to where we would come out. I do anticipate, however, eventual Administration support for an approach along those lines, provided an appropriate revenue source could be identified.

Senator DASCHLE. We are seeking a way to keep this high level of compliance with the diesel tax, while not having taxpayers give the Government tax-free loans. Can you give us some specific suggestions on how that might be done?

Secretary ROSS. Your own bill is one approach. I think to extend it more broadly is going to be difficult if you are talking about actual changes in the collection procedures. because, while those changes would help tax-exempt users, we are concerned they would reintroduce the sorts of evasion schemes that the legislation was initially addressing. As I suggested, there may be approaches along the lines of expedited refund procedures and expansion of the section 6416 procedure, which in effect allows a tax-exempt purchaser to purchase tax-exempt and in a sense assign his refund right to someone else in the distribution chain.

I think those are approaches that may warrant examination but they may each have some revenue consequences that we would, of course, have to take a look at.

Senator DASCHLE. Could not another remedy include a stepped-up audit of the wholesalers themselves by the IRS

Secretary ROSS. The IRS, I think, is currently attempting to improve its audit efforts in this area; and I think in due course that is an approach that would reduce evasion and, in that sense, perhaps permit an expanded ability for certain exempt purchasers to purchase without initially——

Senator DASCHLE. You say they are attempting to do that. How are they attempting to do that? That is contrary to my information.

Secretary ROSS. I believe—and this is my information from the IRS—that they are dedicating additional agent resources to the task of auditing taxpayers in this area

Senator DASCHLE. Could you provide us with some specific information in that regard? It would be very helpful to us.

Secretary ROSS. I would be happy to do that.

[The information appears in the appendix.]

Senator DASCHLE. All right. Mr. Chairman, I have additional questions, but we have another witness. I appreciate your giving me this opportunity.

Senator BOREN. Thank you very much, Senator Daschle. Let me ask just a couple of questions. The Tax Reform Act of 1986 was signed into law in October of that year and I wondered at what point in time did you issue the proposed regulations to implement Section 1703 relating to the gasoline tax excise change?

Secretary ROSS. I don't have the specific date. It was November of last year, Mr. Chairman.

Senator BOREN. So, it was 13 months after the Act was passed that the regulations were issued?

Secretary ROSS. Prior to the effective date but 13 months after the Act was passed.

Senator BOREN. And I understand there have been several clarifications and guidance notices and other changes in regard to those regulations. How many clarifications and guidance notices?

Secretary ROSS. There has been a series; I am not sure of the exact number. They were issued in response to input we received from the affected taxpayers.

Senator BOREN. Would it be a fair estimate to say there have been six or seven additional changes in the form of guidance notices issued?

Secretary ROSS. That sounds about right.

Senator BOREN. So, there is a lot of difficulty with the regulations obviously because of the time it has taken to develop them and the changes that have been necessary. What arrangements have you made to implement the diesel fuel refund procedures? And I wonder how many applications for refund would you anticipate?

Secretary ROSS. I do not know how many applications we are going to receive. I would guess a ballpark figure would be—I can supply that information to you, Mr. Chairman.

Senator BOREN. All right.

Secretary Ross. We have recently issued guidelines that establish what sort of requirements are necessary for the groups that are identified in the statute as eligible to make tax-free purchases. In some cases, those are registration requirements and in some cases not; but that guidance was issued in the last few weeks.

[The information appears in the appendix.]

Senator BOREN. How long do you think it would take to process these applications?

Secretary Ross. I don't know. Perhaps that is a question that I can direct to the IRS and give you an authoritative answer.

Senator BOREN. All right. I would like for us to have in the record as soon as we possibly could the number of anticipated refunds. Are there others here from the IRS who might be able to give us a ballpark estimate?

Secretary Ross. There are people here from the IRS.

Senator BOREN. Two million?

Secretary Ross. Two million.

Senator BOREN. About two million refunds. And I am just thinking of the time it is likely to take to process these and the manpower and so on.

Now, also the gasohol blenders, if they are forced to overpay their gasoline taxes and apply for a refund, the industry is estimating that there could be as many as one million refunds just from the gasohol blenders. Does the IRS agree in general with that estimate?

Secretary Ross. My recollection is that that figure is above what we would anticipate. We were in the neighborhood, I thought, of about 200,000 maximum.

Senator BOREN. You would think about 200,000? How much would it cost the IRS to process those refunds?

Secretary Ross. I think their estimate is around $4.50 per refund.

Senator BOREN. So, we are talking about somewhere over a million dollars in cost?

Secretary Ross. Well, near a million dollars.

Senator BOREN. All right. Thank you very much. We will turn now to Mr. Robert Farris, the Administrator Designate of the Federal Highway Administration I believe you have with you Mr. McMahon, who is the Chief Counsel.

Mr. FARRIS. The Chief Counsel, yes.

Senator BOREN. And we are happy to have both of you with us, and we will be happy to receive your full statement for the record. You can feel free to abbreviate your statement if you wish.

STATEMENT OF ROBERT E. FARRIS, ADMINISTRATOR DESIGNATE, FEDERAL HIGHWAY ADMINISTRATION, WASHINGTON, DC, ACCOMPANIED BY ANTHONY J. McMAHON, CHIEF COUNSEL

Mr. FARRIS. I will be brief, Mr. Chairman. I will be submitting my full statement for the record, if you please.

You know, I am in somewhat of an awkward position today because we don't collect taxes; we try to use them. Our principal concern is to see that those taxes that are duly paid for use of the consumption of fuel in this country are appropriately transferred to the Treasury and subsequently to the Highway Trust Fund.

Evidence was strong, to us, over the last several months, and to former Administrator Ray Barnhart, that there was considerable loss of highway tax revenue in the whole process; that there were taxes actually either being paid and then diverted, or, in fact, actually being evaded in the process.

And the audit trail was quite difficult to keep up with. So, we are quite a strong supporter of trying to improve the collection of the highway use taxes from those who ought to be legitimately paying them. It was not the intent of this Act or the Administration or anyone else to put any undue burden on those who are legitimately authorized to consume this fuel on a tax-free basis.

I believe what we have got here is an implementation problem, rather than an intent problem. We can reasonably look to an improvement in the receipts in the Highway Trust Fund as a result of this Act. And I think, to say that, is a benefit to the general public; that taxes that are supposed to be paid and are obligated to be paid and, in fact, in some instances are paid, may not be finding their way into the Highway Trust Fund.

So, with that intent, the new legislation to raise the point of taxation is proper and we strongly support it. We hope that we don't throw the baby out with the bathwater here, as we try to work with those who have legitimate tax-exempt authority or who can properly exercise that authority. At the same time, we must tighten up the collection process so that the funds that are properly due to the Highway Trust Fund are in fact paid.

So, I am here to champion the cause of the Highway Trust Fund and not to put any undue pressure on anyone who has a legitimate exemption purpose.

I was just down in New Orleans recently and heard this same argument from the Associated General Contractors, where they are concerned that fuel that they purchase for off-the-highway use for their road machinery are having to go through the same process.

But it appears to me that the increased number of exemptions may in fact be processed—that is, be used—for evasion. We need to look very carefully at that whole process, not that farmers and other people who have proper claims on the consumption of fuel on an exempt basis ought not to continue to do so.

It is the process that we are concerned about; and the more exemptions you put in the stream, the more opportunity you make available for evasion.

On the other side of the coin, we have proposed in our budget this year—the 1989 budget—a $5 million item that we will make available to the Internal Revenue Service to assist in this improved audit. Senator Daschle, you brought that question up on how they were going to improve their auditing.

There is additional cost for that. We think it is a wise investment on our part to pay for increased enforcement effort out of the Trust Fund when, in fact, we believe that the evasion exceeds $1 billion a year, not the conservative estimate that the Treasury is using for budget estimates.

All of those are simply estimates on our part, but in looking at what has happened in other key States where they have adopted similar measures, we have seen dramatic increases from their collection procedures, up as high as 20 to 30 percent improvements.

So, taking that as a measure, and taking what we do receive into our Trust Fund, I think a billion dollar estimate is a legitimate estimate that we should take steps to recover without imposing any additional burden on those who have legitimate claims for tax-exempt consumption.

The process is a difficult one, and we recognize that. We would urge that you and the rest of Congress move cautiously as you hear the concerns—very legitimate concerns—and as we try to implement our intent of getting into the Trust Fund all of those dollars that ought to legitimately be paid; and we strongly support that.

You will hear us speak out on behalf of the Trust Fund as much as possible, but the actual implementation responsibility is Treasury's and as a sister agency, I would not sit here today and try to describe to you how that ought to be done.

So, with that, I will conclude my testimony, Mr. Chairman, and I will be glad to respond to any questions.

Senator BOREN. Thank you very much, Mr. Farris. Mr. McMahon, anything that you wish to add to Mr. Farris' statement?

Mr. MCMAHON. No, sir.

[The prepared statement of Mr. Farris appears in the appendix.]

Senator BOREN. Let me ask a question. You talked about the implementation problems. Do you have any suggestions for us as to how we might deal with this implementation problem?

Mr. FARRIS. I have one personally, if I might pass it along. One of the things we have talked about and I have had some conversation with the Treasury, is to set up a pilot project to see if we can't assist States to let them, as they collect their taxes, to collect ours.

It seems to be a very legitimate approach. They are on the firing line. They have demonstrated to us in many instances—and my home State of Tennessee being one of them—that they can in fact improve the collection process. So, it ought to be worth our considering, together, to allow a State, at the same time if they have the same collection points that we do, while they are picking up their State tax, that they also pick ours up and provide them some payment for that process.

It appears to me to be something we ought to legitimately consider. It is not a new idea. Ray Barnhart discussed that with some of you earlier and I think it is something that we ought to honestly look at.

Beyond that, I would be infringing upon my sister agency to get into the tax collection business. I build highways and repair bridges and other sorts of things, but that is a thought that I think we ought to legitimately chew on. It has a lot of merit, in my judgment.

Senator BOREN. Let me ask something on an unrelated matter; but since you are here, I can't resisting asking. On these new regulations on commercial operators' licenses, is that Federal Highway Administration regulation?

Mr. FARRIS. Yes, sir. You bet.

Senator BOREN. It is due to go into effect on the 15th of July; is that correct?

Mr. FARRIS. We will issue the final rule, which will establish the minimum testing standards and the driving standards that States must adopt by 1992. So, it will be a rather lengthy process but we

will have the final rule out setting those minimal standards by July of this year.

Senator BOREN. So, States have until 1992 to adopt the implementing legislation?

Mr. FARRIS. Yes, sir.

Senator BOREN. But as I understand this as we have been reading this it could require people with even small vehicles like pickup trucks, if they happen to carry fertilizer in their operations of fuel, to have these operators licenses. Is that correct?

Mr. FARRIS. Yes. There are provisions in the Act that require those who have sufficient quantities of material that require a placard on their truck, that they would have to have a commercial license. Anhydrous ammonia is one that comes to mind, and farmers use a lot of that.

There are also exemption provisions that we are looking at very carefully. As we went out on the street with a Notice of Proposed Rule Making, we had a flurry of statements presented to us; they are all under analysis now. We think we can reasonably deal with those issues.

It is not our intent, and I don't think the intent of Congress, to unnecessarily burden the people in the United States with this; but it was an intent to improve the quality of drivers who operate large vehicles in our system and to have them demonstrate that they at least have some skill for the kind of vehicle that they are operating, plus providing us a mechanism to remove the problem drivers from our system.

We are trying to do that. You know, volunteer firemen, I am sure, have said the same thing to you. I have a great respect for the volunteer fireman; many times they love their fire engines more than they do their wife. I don't see any real problem in excluding volunteer firemen.

But there are certain categories of exemptions that ought to be honestly looked at; and you have mentioned one of them here this morning.

Senator BOREN. I would urge you to consider those very, very carefully before you issue the final regulations. We would hate to have to pass an appropriation to improve the security force at the Federal Highway Administration to protect you against the public response that might come from the regulations that are drafted.

Mr. FARRIS. I appreciate that.

Senator BOREN. So, being one concerned for the Federal Highway Administration, let me urge you to take another look at those before they are finally issued because there are certainly a number of us here looking at them. Senator Daschle?

Senator DASCHLE. I would just add to that that since it is already regulation that all motorcycle riders have helmets, I would suggest the Administrator consider one as well. [Laughter.]

Mr. FARRIS. Or some shin guards.

Senator DASCHLE. That is correct. I would have only one other point, and I know we have a vote on, that I would ask Mr. Ross. Mr. Ross, the number of governments representing populations of under 3,000 in this country is really significant—28,484. We have 331 of them in Oklahoma; 1,250 of them in South Dakota. If just one percent of those governments were to ask for a refund on an

annual basis, my view is that the cost/benefit ratio, the effect of this, could be very problematic in terms of the numbers that you presented earlier in your testimony in collection.

Do we save money? Has the Treasury actually done a cost-effectiveness analysis with regard to the collection and the prospective refund potential that exists among these small communities—28,000 plus?

Secretary ROSS. I do not know if the estimates I referred to in my testimony are net of administrative costs, but that is the kind of information I would be happy to supply to you. Presently, we have made a judgment that, while there will be clearly some administrative costs additionally for the IRS, indeed a cost for the affected local governments

Senator DASCHLE. You would agree, wouldn't you, that that is a significant question? I mean, obviously if you are talking gross or net in the figures you cited, it brings a completely different perception to the revenue argument that you have made that was one of the central parts of your testimony. Do you have that information to be made available to us right now?

Secretary ROSS. No, I don't have it with me, but again, that is something that we can supply. I don't deny that that is a significant question. I don't think that the administrative cost is going to approach really very substantial compliance gains but you are right certainly to raise that question. And we will get information to you that is responsive.

Senator DASCHLE. Would it be possible to get it to us before the markup on Friday?

Secretary ROSS. Certainly.

Senator DASCHLE. Very good. Thank you, Mr. Chairman.

[The information appears in the appendix.]

Senator BOREN. Thank you very much. Now, as I understand it, Mr. Ross—and I apologize that I had to go and vote during part of your testimony—the White House does have this matter under review—under active review.

Secretary ROSS. That is correct.

Senator BOREN. And there is not an official position yet.

Secretary ROSS There is not an official position yet. I am hopeful certainly of having one in time for the Friday markup.

Senator BOREN. That is what I was going to stress, that I hope there will be a position from the Administration. We obviously hope it is going to be an affirmative and positive position from the Administration.

Secretary ROSS. As I said, that is my expectation. They are well aware of the Friday timetable.

Senator BOREN. Right. Thank you very much. I am going to ask our next panel to stand by a few moments. Unfortunately it appears they are going to have a whole rash of votes on the floor; and this one is only a 15-minute roll call. So, we are going to have a brief recess.

Before we do, I would like to introduce Mr. S.M. True and the remainder of our next panel—if they would come forward—Mr. S.M. True of the Texas Farm Bureau and Member of the Board of Directors of the American Farm Bureau Federation; Mr. Daniel Scherder, Vice President for Financial Administration of Peabody

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Holding Company, Incorporated, testifying on behalf of the National Coal Association and the American Mining Congress of St. Louis, Missouri; Mr. Timothy Columbus, Counsel of the Society of Independent Gasoline Marketers of America; Mr. James Day, President and Chief Executive Officer of Noble Drilling Corporation, testifying on behalf of the International Association of Drilling Contractors and the Association of Oil Well Servicing Contractors, and also on behalf of the International Association of Geophysical Contractors of Tulsa, Oklahoma; and Mr. Jack Kelsey, the President of the Oklahoma Farmers Union, Oklahoma City.

We are very glad to have all of you. Also, Don Schieber, President of the Oklahoma Wheat Growers Association is with us as well. Don, we are very glad to have you with us this morning.

We will have to take just a very brief recess. I will vote and come right back and we will resume; or if Senator Daschle gets here before I get back, he will resume. I thank you for your patience and understanding. We will have just a brief recess, and then we will resume with this panel.

[Whereupon, at 11:05 a.m., the hearing was recessed.]

AFTER RECESS

Senator BOREN. We will resume at this point. I appreciate the patience of the panel and our guests. Let me also say that Senator Danforth had hoped to be here this morning and also wanted to enter into the record a statement by Mr. Joseph Farrell, President of the American Waterways Operators.

[The statement of Mr. Farrell appears in the appendix.]

Senator BOREN. I think we will just start down the row in order here. We are pleased to have all of you come today and we know that some of you have come from great distances; and we look forward to hearing your testimony.

Mr. Day, we will begin with you.

STATEMENT OF JAMES C. DAY, PRESIDENT AND CHIEF EXECUTIVE OFFICER, NOBLE DRILLING CORP., TESTIFYING ON BEHALF OF THE INTERNATIONAL ASSOCIATION OF DRILLING CONTRACTORS, ASSOCIATION OF OILWELL SERVICING CONTRACTORS, AND INTERNATIONAL ASSOCIATION OF GEOPHYSICAL CONTRACTORS, TULSA, OK

Mr. DAY. Thank you, Mr. Chairman and Senator Daschle. My name is Jim Day, and I appear today on behalf of the International Association of Drilling Contractors, the Association of Oilwell Servicing Contractors, and the International Association of Geophysical Contractors. We run the gamut in the oil business. We go from going out and trying to find oil to drilling it and subsequently producing it and keeping it producing.

I am President of Noble Drilling Corporation; we are headquartered in Tulsa, Oklahoma. We are involved in both offshore and land drilling activity.

Rather than read this statement verbatim, I understand, Mr. Chairman, that the full statement will be included in the record.

Senator BOREN. We will enter the full statements of all of our witnesses today into the record. So, feel free to summarize and hit those points that you think are most important for us.

Mr. DAY. Thank you. Very good. The IADC represents virtually all the drilling businesses in the United States, about 1,200 companies. The AOSC represents about 650 companies; the geophysical group, the IAGC, represents 160 companies.

As I indicated, we are very concerned about the fuel tax, its effect and the change in the tax. As we understand it, the change in the collection procedure occurred under the Omnibus Budget Reconciliation Act of 1987.

And reflecting on that, I doubt if it were brought out as a free-standing issue whether it would have passed public scrutiny at that point in time; but nevertheless, it is here, it is real, and it is going to cost our organizations' members a lot of money.

Now, as we understand it, the Internal Revenue Service has not argued with the fact that we are exempt from it. That wasn't the issue; but it is coming up on April 1, and the actual effect on us is dramatic.

One of the critical things that has happened to our business, like the farmers, in the last five years—because it is of a very cyclical nature also—is that there were over 5,500 rigs in the business five years ago; today, there are 3,000. Of those 3,000 rigs in the drilling group, less than 1,000 are working—30 percent; and they are not making any money.

It has been estimated that, of the total drilling group, there are only two that have made any profit; and I would surmise that, if you looked at that drilling group, it is probably profits from some other source of revenue rather than the drilling operation.

We are in an anemic state. I don't have to apprise you of that. You are very cognizant of that.

In any case, let me differentiate; we do not as a drilling contracting group participate in the production of oil and gas. We just drill the holes. Therefore, we don't have guaranteed revenues coming in from the production.

Our business is highly cyclical; and as I indicated earlier, there are just a few companies that have had a profit. The average land rig today uses about 290,000 gallons of diesel fuel per year. If you extrapolate that out at 60 cents per gallon, you can see it is a significant amount of money, $170,000 to $180,000 per unit.

Offshore rigs use 612,000 gallons of diesel fuel in a year; that is $360,000 and more per year per unit: significant dollars.

For well-servicing contractors, only 54 percent of the existing 6,200 units are working. Much like the drilling rigs, the well-servicing rigs use about 25,000 gallons of fuel; again, that's $15,000 annual tax that they would have to pass through.

It is the time value of money that these people are faced with, money that they don't have. In the geophysical group, there are 175 crews working today, a fraction of what occurred just six years ago. There were 741 crews working at that point in time.

Extrapolating from the current on shore seismic crew count from what is occurring today, the geophysical industry consume approximately 1,700,000 gallons of fuel annually.

For marine seismic work, there are 30 geophysical vessels operating in U.S. waters. Those 30 units consume about 1,800,000 gallons of diesel fuel annually.

What is difficult for us to understand is that all contracting drilling work is done on a stationary location; certainly, we travel between locations, but the preponderance of the work is on-site location. It is not on the road. They don't drill on the highway. They are at remote locations.

And it also is applicable to the seismic work. Seismic work is done in very remote areas, searching for new horizons for gas and oil.

I will make two brief comments. It is difficult—almost absurd—for me to understand and the members of our industry to understand why this is occurring, this new tax collection. This industry—and I am speaking of all three entities—is not operating off of profits or retained earnings. They are operating off cash flow, and many of them don't have cash flow, much like the farming group.

This is just another load that will prove to be the death knell for our industry, this additional cash flow loss that we would experience.

I would urge this subcommittee and certainly the full Senate Finance Committee to quickly remedy this unfair tax change.

Thank you for the opportunity to represent the oil field service group today.

Senator BOREN. Thank you very much, Mr. Day. You are certainly right. If we were to try to sit down and design a tax burden that would be regressive and put it on those industries that could least afford it, here we have the whole oilfield service industry in a terrible depression—that is the only term that you can use. We have the farmers, certainly in the Plains States, in a depression, barely hanging on.

We have commercial fisheries in severe trouble. And here we go and put a tax burden on those elements of our society and our economy that can least afford to bear it, as you say.

I talk to people every day who say: When am I going to have cash flow enough to stay in business another week, another two weeks? It is true with the oil industry, and especially the service side of it; and it is certainly true in agriculture as well.

And here, we come along and put an additional burden on that cash flow. It makes no sense. I appreciate your comments, and they are going to be very helpful to us in getting this matter changed.

Senator Daschle, any questions?

Senator DASCHLE. No questions, Mr. Chairman.

Senator BOREN. I might ask: Typically, do the drilling contractors purchase diesel at retail or wholesale levels?

Mr. DAY. Generally wholesale. It depends on the size. You have to understand that of the 1,200 members we have, most of them have five rigs or less. Many of them try to buy on a wholesale level, but some buy on retail.

[The prepared statement of Mr. Day appears in the appendix.]

Senator BOREN. Right. Thank you very much. We will hear now from Mr. Dan Scherder, representing the American Mining Congress.

STATEMENT OF DANIEL B. SCHERDER, VICE PRESIDENT, FINANCIAL ADMINISTRATION, PEABODY HOLDING CO., INC., TESTIFYING ON BEHALF OF THE NATIONAL COAL ASSOCIATION AND THE AMERICAN MINING CONGRESS, ST. LOUIS, MO

Mr. SCHERDER. Thank you, Mr. Chairman. I am Dan Scherder the Vice President of Financial Administration for Peabody Holding Company in St. Louis, and I am Chairman of the American Mining Congress Tax Committee. I am appearing here today on behalf of the American Mining Congress, as well a the National Coal Association.

The American Mining Congress is an industry association representing all segments of the mining industry It is composed of U.S. companies that produce most of the Nation's metals coal; and industrial and agricultural minerals; companies that manufacture mining and mineral processing machinery and equipment; and engineering and consulting firms, and financial institutions that serve the mining industry

The National Coal Association is a trade association composed of about 200 members directly or indirectly representing about 90 percent of the coal producers in America.

In addition, the coal producing companies in NCA's membership include coal brokers, equipment suppliers, coal transporters, consultants, electrical, utilities, and resource developers.

We appreciate the opportunity to present our views on the repeal of the up-front exemption from the Federal diesel fuel excise tax for fuel purchased for off-highway use. The stated purpose of the 1986 Act was to prevent the evasion of the diesel fuel excise tax.

In fact, however, for users of diesel fuel for exempt purposes—such as the mining industry, which is a major user for exempt purposes—the repeal is nothing more than a forced interest-free loan to the Government.

Because the American mining industry is a substantial user of diesel fuel, this involuntary loan provision will have a very onerous impact on the industry.

Diesel fuel is used in the mining industry to power a multitude of different types of equipment, from trucks to drag lines to engines used to run standing equipment and to run some underground mining equipment.

These uses of diesel fuel are not highway uses and, accordingly, are not and have not been subject to the diesel fuel tax. Nevertheless, the provisions of the 1987 Act would require the mining industry to pay the Federal diesel fuel tax on all the fuel it purchases for these exempt purposes.

Like everyone else—the farmers, the drilling industry, et cetera—in order to get our money back from the Government, the industry will have to go through the additional record keeping and administrative burdens associated with pursuing refund claims from the Government.

And finally, as the others, it will receive no interest for this loan.

The onerous impact on the mining industry can be best illustrated by the impact on the coal segment. The Pennsylvania Coal Association has estimated that approximately two to four gallons of diesel fuel are used in the mining of one ton of coal. The Associa-

tion further estimates that the repeal of the off-highway use exemption would reduce the cash flow of the coal mining industry in Pennsylvania by about $6 million.

If you take this for the U.S coal mining industry as a whole, it means about $100 million annually. If you take this even further for the U.S. mining industry, it is somewhere in the neighborhood of $250 million annually.

There are other additional costs that the repeal of the off-highway exemption will impose on the domestic mining industry. The coal segment of the industry moves approximately 20 percent of its product through the inland waterway barge system.

Since the repeal of this exemption would also increase the cost of barge operators, the cost of this type of transportation will rise.

Since the early 1980s, the U.S. mining industry has been in a depression, as have the farmers and the oil people. During this period, the size of the industry has declined. The industry has been subjected to competition from producers that are wholly or partially owned, operated or subsidized by foreign governments.

A reduction of the industry's cash flow that will result from the repeal of this exemption is yet another complicating factor in the industry's efforts to regain its strength and its ability to supply the minerals needed for the nation's economy and for its national defense.

Also in the last five years, there have been onerous tax provisions placed on the mining industry. With the 1986 Act, the mining industry actually had a substantial increase in tax burdens, where other industries actually had decreases.

We applaud the efforts of the Senators and Congressmen who are pressing legislation to restore this very important up-front exemption and the efforts of the Finance Committee for the markup session which is scheduled to address this issue.

If corrective legislation cannot be enacted by April 1, the effective date, then legislation should be enacted simply postponing that effective date until appropriate corrective legislation can be devised and enacted.

The American Mining Congress and the National Coal Association appreciate the subcommittee's concern with this issue and its willingness to examine it. We sincerely hope the subcommittee and the Congress realize the magnitude of the mistake which was made in the 1987 Act and ask that they act promptly to correct it.

Thank you again for this opportunity to present our views.

Senator DASCHLE. Thank you, Mr. Scherder. That is excellent timing. [Laughter.]

Did you rehearse that?

Mr. SCHERDER. No. Blind luck. [Laughter.]

Senator DASCHLE. You testified that the industry would lose about $100 million—if I heard you correctly—because they are going to have to pay the diesel tax up front and then file for the refund of that tax. We understand that companies can reduce their estimated tax and individuals can adjust their withholding by the amount of their expected refund in order to reduce the out-of-pocket costs of the tax.

Does this ability to reduce the current tax payment help offset the total cost of the tax to your industry?

Mr. SCHERDER. Senator, the $100 million number was the cash flow impact. The ability to do it on a quarterly basis would reduce the cash flow impact, but it would not offset it because there would be a three-month period where you pay in the tax before you even file for the refund.

We have heard testimony on the length of time it would take to get the refunds. It would be a very onerous cash flow impact because you probably are looking at a three-month minimum and possibly a six to nine or twelve month time frame when the Government would be using our money, interest-free.

Senator DASCHLE. Would you like to see more frequent filings of refunds and interest?

Mr. SCHERDER. I am not so sure that that would alleviate the problem because more frequent filings would raise the burden of the IRS, and I still think it would be an extremely long period of time before they could process the refunds, plus it would be a larger administrative burden on the companies of having to file more often.

[The prepared statement of Mr. Scherder appears in the appendix.]

Senator DASCHLE. Thank you, Mr. Scherder.

Senator BOREN. Thank you very much.

We will hear now from Mr. S.M. True, President of the Texas Farm Bureau. We are very happy to have you, Mr. True.

STATEMENT OF S.M. TRUE, PRESIDENT, TEXAS FARM BUREAU, AND MEMBER, BOARD OF DIRECTORS, AMERICAN FARM BUREAU FEDERATION, PLAINVIEW, TX

Mr. TRUE. Thank you, Mr. Chairman and Senator Daschle. My name is S.M. True. I am a farmer and a rancher from Plainview, Texas. I operate a medium-size cotton, wheat, feed grain, and cattle operation. I also serve as President of the Texas Farm Bureau. Today, I am also representing the American Farm Bureau Federation, the nation's largest organization of farmers and ranchers.

On behalf of all farmers, I want to thank you for holding the hearings.

I am here today to share with you the Farm Bureau's concern over the obscure provision of the Omnibus Budget Reconciliation Act of 1987, which will have a profound impact on millions of farmers and ranchers. This provision changes the collection point for diesel fuel tax from the retail level to the wholesale level and, beginning April 1 of this year, farmers will be forced to pay a 15 cents per gallon excise tax on diesel fuel and then file for a refund or a credit.

Today, we are asking your favorable consideration of legislation that will permit farmers and ranchers to continue to buy fuel tax-free, if it is to be used for off-highway purposes. If this provision is not changed, farmers and ranchers will be burdened with an additional operating expense which will total hundreds of millions of dollars in diesel fuel excise taxes.

Although farmers will be able to apply for a refund of these taxes, cash flow problems and higher interest costs to agricultural

producers will undoubtedly result. The cost to agriculture would be substantial.

According to the 1982 Census of Agriculture, annual farm diesel fuel use is approximately three billion gallons; and at 15 cents per gallon, agriculture producers will be forced to pay approximately $425 million in diesel taxes.

In my home State of Texas the impact on agriculture would be about $30 million; and on my particular farm, which is a fairly typical operation, my off-road diesel fuel consumption per year is approximately 8,346 gallons.

This means that I will be forced to pay about $1,250.00 in taxes to the Federal Highway Trust Fund for the diesel fuel used off the highway on my farm in the production of crops and livestock.

Included in my statement for the record are State farm diesel fuel use figures for the 1982 Census of Agriculture. These statistics dramatize the impact of this new tax on farmers nationwide. This is a tax that farmers do not owe and should not have to pay.

It means that I must borrow additional operating capital, that I will have higher interest costs. It means additional regulation paperwork to obtain a refund. The timing couldn't be worse.

This new expense and regulatory burden will be imposed when farmers must cut expenses and increase efficiency just to survive. Although many of the details of the refund system to be imposed are not yet clear, there may be some major inequities.

The Internal Revenue Service has informed us that farmers may file for a quarterly refund if the refund for the quarter is $1,000 or more. This would require diesel fuel use of at least 6,666 gallons per quarter, or 26,666 gallons per year.

Now, only the very largest farms use this much diesel fuel. In a check with the United States Office of Energy, we have estimated that less than 20,000 farmers would qualify to file for quarterly refunds. Most would have to wait until the end of the tax year to file for a tax credit on IRS Form 1040.

And to make matters worse, no interest would be paid by the IRS for payments held prior to refund. In effect, we farmers will be making interest-free loans to the Federal Government. We think this is ridiculous. Ironically, the cost to the IRS of distributing and maintaining a refund system may outweigh the benefits of the revenue which may find its way to the Treasury.

And last, we would like to bring to your attention a problem which underscores the need for quick legislative action to restore the previous tax-free purchase method of diesel fuel for off-highway use.

An excise tax for off-road diesel fuel could increase fuel costs and disrupt the distribution system. This could occur when farmers and other off-road users top off their storage tanks before April 1 to avoid paying the extra 15 cents per gallon.

This could create sudden, artificial demand for billions of gallons of diesel fuel, which could not be supplied by the current refining and distribution system. This problem could be especially serious since it would take place in the early spring, the peak fuel use period for off-spring planting.

I would like to also inject that just last Saturday, I received a letter from a local distributor telling all their customers that the

tax would go into effect April 1 and there would be an additional 15 cent cost on their bills. And he also is recommending that everyone top off their tanks prior to April 1, if it is possible.

Mr. Chairman and members of the subcommittee, the new requirement for collection of farm diesel fuel taxes is unfair. It is a questionable benefit to the Federal Government, and it will create a new financial and regulatory burden on farmers and ranchers. It will increase production costs and may cause serious disruption in fuel supplies which are essential in the production of agricultural commodities.

There have been a number of bills introduced, one by Senator Daschle, S. 2075; and I think it will solve the problem. There have been a number of other bills introduced. I think we have 50 as of yesterday, 51 who have signed on the Senate side and 218 on the House side.

We appreciate the effort you fellows are making in trying to deal with a very serious problem for agriculture. I have faith in the system.

We thank you very much for listening to us.

Senator BOREN. Thank you very much. We hope to keep faith with that. We understand sometimes how you might have a few questions when these kinds of helpful things are done to you.

You certainly make a good point about the total economic impact and also the fact that the frequent refunds would only be available to those high-volume, very large operators. So, the small farmer who experiences the acute cash flow problem would not be able to get any kind of assistance under this refund policy.

How do you respond to the suggestion of the Federal Highway Administrator that we might have more frequent refunds? How do you react to that?

Mr. TRUE. No, sir. That just creates more paperwork, more concerns for the farmers and the ranchers out there. Personally we feel like they are just stealing money from us, in the first place.

Senator BOREN. I wouldn't quarrel with that description at all. [Laughter.]

Senator Daschle, any questions?

Senator DASCHLE. No questions, Mr. Chairman.

Senator BOREN. Thank you very much, Mr. True.

Mr. TRUE. Thank you, Senator.

[The prepared statement of Mr. True appears in the appendix.]

Senator BOREN. We are very happy to have with us this morning also a man who has been an advisor to me on agricultural matters for a long time, and I am appreciative of his taking time to come. Mr. Jack Kelsey, the President of the Oklahoma Farmers Union. We are really appreciative of your being with us today.

STATEMENT OF JACK KELSEY, VICE PRESIDENT, NATIONAL FARMERS UNION, AND PRESIDENT, OKLAHOMA FARMERS UNION, OKLAHOMA CITY, OK

Mr. KELSEY. Thank you very much, Senator Boren and Senator Daschle. My name is Jack Kelsey and I am President of the Oklahoma Farmers Union; and last week, Senator, I was elected National Vice President for the National Farmers Union, a general

farm organization of 250,000 farm and ranch families throughout the United States.

We certainly appreciate this opportunity to present the Farmers Union views on the very important issue of collection of diesel fuel taxes.

In the convention last week, local elected delegates debated and passed the following special order of business unanimously, and I must say it was probably the number one topic of discussion; and that was Article 12, Special Order of Business, adopted by delegates to the 86th Annual Convention of the National Farmers Union in Albuquerque, New Mexico, on March 9, 1988, titled "Repeal of Provision Imposing an Excise Tax on Farm Diesel Fuel."

Congress must act before April 1, 1988 to assure that U.S. farmers do not become the costly victims of a deficit reduction ploy in the Budget Reconciliation Act adopted by Congress last December.

That statute imposed a 15 cent a gallon excise tax on farm diesel fuel beginning on April 1, 1988.

It was estimated that the tax would raise $420 million in revenue, but it would not cost farmers anything because they could file for refunds later, perhaps when they file their next returns.

However, the new tax would require farm operators to pay 20 percent more for their diesel fuel at planting time and then wait several months or perhaps near to a year to obtain a refund.

For many farmers, this imposition of the diesel tax will aggravate cash flow problems which are already serious. So, this is a needless $420 million in punishment for the U.S. farmers, particularly in view of the fact that there is no real long-term deficit reduction that will be achieved.

The view we express today is shared by the National Farmers Organization, the American Agriculture Movement, the National Save the Family Farm Coalition, and the League of Rural Voters, and of course, the wheat growers.

The change in the collection point of the diesel point has, in my opinion, universal opposition of all the farm group representatives with whom I have had the opportunity to talk.

Mr. Chairman it is very seldom that changes put forth by Congress miss the mark, but this diesel tax collection will, in our opinion cause great problems and financial stress will impact all the parties concerned.

The small farmer, who is under the greatest financial strain, will be forced to borrow more money to pay the 15 cents per gallon tax on fuel that he used off-road in his normal farming operations. This fuel historically has been exempt from the road use tax and it is the intent that it will be exempt in the future.

However, due to budget reconciliation number shuffling, this tax will be collected and then returned to the farmer at some future time. Larger fuel buyers will be inconvenienced for as little as 30 days; small farmers will borrow money and in effect lend it to the Government interest-free.

At first, it appears that the Government has a great windfall. On closer analysis, it is obvious that even the Government loses when the cost of the paperwork is calculated. The added expense of borrowing the money by farmers is tax deductible; therefore, the U.S. Government is the ultimate loser.

It is reasonable to assume that it will not be long before the individual States will decide that early collection is the logical step. What started out as a program to catch a few tax cheats will cost the small family farmer 25 percent more for his farm fuel.

He needs to borrow more money at a time when he is having trouble repaying what he already owes; this does not seem to be the way to go.

Mr. Chairman, the American farmer wants to pay his fair share. We are ready to do what is necessary to get our financial house in order. To continue a tax collection program where all parties concerned lose is senseless.

We think there is still time for reason to prevail and the problem can be rectified. The United States Senate must show that, when mistakes are made, the leadership can and will pass correcting legislation in time to prevent needless problems.

Agriculture has had more than its share of difficulty in the past few years. Mr. Chairman, the Farm Credit Act that was passed with your guidance was a great step towards the recovery of rural America, and the correction of the problem in front of us today will also help in that recovery.

I want to thank you again, Senator Boren, for the opportunity to be here.

Senator BOREN. Thank you very much, Mr. Kelsey. I appreciate your comments, and you certainly expressed the problem very well. Thank you also for your comments about the Farm Credit Bill.

Let me say that Senator Daschle, who is here with me today, also is a member of our subcommittee on the Agriculture Committee; and he was a great help to me in the writing of that legislation. More and more, we are getting a few crossover members between the Agriculture Committee and the Finance Committee; and those of us who happen to come from agricultural areas think that is a very positive development. We appreciate your testimony very much today.

We are glad to see that we have a Texan and an Oklahoman sitting there together. We have united on this issue. We have been at peace now between Oklahoma and Texas for over 50 years now, ever since Oklahomans chased the Texas Rangers off the bridges and won the border war. [Laughter.]

I just want to put that in the record, when Senator Bentsen wasn't here to hear it because he may come in and try to correct the record after he hears that. [Laughter.]

[The prepared statement of Mr. Kelsey appears in the appendix.]

Senator BOREN. We will hear now from Mr. Timothy Columbus, who is representing the Society of Independent Gasoline Marketers of America. Mr. Columbus, we are glad to have you.

STATEMENT OF R. TIMOTHY COLUMBUS, COUNSEL, SOCIETY OF INDEPENDENT GASOLINE MARKETERS OF AMERICA, WASHINGTON, DC

Mr. COLUMBUS. Thank you, Mr. Chairman and Senator Daschle. My name is R. Timothy Columbus. I am a member of the law firm of Collier, Shannon, Rill & Scott; and I appear today on behalf of

our client, the Society of Independent Gasoline Marketers of America.

While my testimony addresses several points, there are three upon which I would like to primarily focus today.

First of all, that those provisions of the Budget Reconciliation Act of 1987 which provide for a change in the collection of diesel fuel should be repealed. I am sympathetic with your efforts to amend this to deal with specific problems; but as my testimony will discuss in greater detail, I think that you are only starting to scratch the surface on what was wrong with that whole idea.

Second, I will urge the subcommittee and full committee to enact legislation that is similar to that proposed by Congressman Pickle in the Technical Corrections Bill passed out of the House Ways and Means Committee last year to deal with two problems. One is a competitive problem, a competitive in equity in dealing with State and local government entities in the gasoline industry; and also to ensure the continued viability of gasohol.

Finally, I urge you to take back to your colleagues that Congress should make a very simple investment in an effective deterrent to tax evasion; and that is not going to happen by restructuring the system. It is going to happen, plainly and simply, by capital investment in computers, in personnel to deal with data submitted by the industry; and my client believes that Congress can work effectively with the petroleum industry and the IRS to put together a program to ensure you get the data and discover tax evasion on a prompt basis.

Now, with request to the repeal of the diesel fuel tax changes, I would say the purpose was clear, and two-fold. First, increase revenues really from two sources. One we are going to increase our float.

People all day have told you it is their money and it was a real bad idea.

The second thing is we are going to cut down on evasion. Mr. Chairman, I submit that evasion in the diesel fuel tax system is not going to be decreased by these changes; it is going to be increased. It is very simple.

What you have done plainly and simply is recreate the very system for tax collection that gave the IRS and the Highway Administration such concern in the Harbor of New York City. We changed the gasoline excise tax collection system to get away from the system that Congress has now put in place for the diesel fuel tax.

And I am mystified by how people who are as smart as you all are normally can do anything that silly. [Laughter.]

The second problem you have to recognize is that all diesel fuel is home heating oil. So, you are going to have an opportunity for people to move in volume now—in volume—number two distillate fuel. And we can just buy it as home heating oil and a disreputable guy can sell that off as diesel fuel. He is going to pocket 15.1 cents and in the motor fuels business, that is a ton of money.

The second thing is he will buy diesel fuel—brilliant. He will then put together that same string of shell corporations, that little daisy chain; and they are going to be tax exempt when he buys it.

And by the time it comes out of that daisy chain, it is going to be tax paid.

In the old days you had two kinds of taxpayers—honest ones and dishonest—people who didn't pay their taxes. But what you are going to have now is people who formerly paid their taxes—honest retailers—being offered what I refer to as "deep discount diesel fuel" by tax-cheating wholesalers.

They are going to be offered it, saying this is tax paid. They are going to buy it; they are going to have to because the competitive pressure in the retail market that tax cheating is going to generate is going to force them to do it.

In short, not only are you taking other people's money, but I think you are going to lose revenues. You know, you came here to drain the swamp, Senator; and all I can see so far is you have dug a channel uphill that, when it rains, is going to put more water in the swamp rather than take it out.

With respect to gasoline excise tax problems, there are only two things I would ask you to remember. First of all, because of the new tax collection system, many marketers buy on a tax-paid basis. That is going to limit their ability to service the business of State and local governments.

The legislation proposed by Mr. Pickle not only would take care of that problem; it would also deal with gasohol blenders.

Now, SIGMA's members sold about 4 billion gallons of gasohol last year. It is an important competitive tool. It is an important market for American producers of agricultural products. And I think you ought to take a look at that and make sure that goes on and that problem gets resolved

My final pitch for the day, Senator, is buy yourself a computer. Now, that is going to be a big computer, and you are going to have to work with the petroleum industry to put together a reasonable reporting program; but a lot of that is in place now.

There is a system out there now called Petro-X where we get a lot of data now right off of the terminals. That is the only way you are ever going to stop tax evasion. It is the only credible deterrent.

The amount of money involved here just convinces me that where there is going to be a will to cheat, there is going to be a way to cheat. The computer is your best bet.

All legitimate business people hate tax cheating. They pay at least as much out of the market price of their products as the Government loses. We would like to work with you to solve that problem, but let's do it in a way that is likely to get us out of this morass

Thank you.

Senator BOREN. Thank you very much. You have made some excellent suggestions; and I think your point that we are going to likely increase evasion rather that increase compliance with the way that this has been done is a very good one.

Your point about the interchangeability of heating oil and diesel is another point that is important to keep in mind.

I understand the Canadians even put red dye into that or take some other action to deter this.

Mr. COLUMBUS. Senator, let me respond to that very quickly. Somebody looked up at me and they said: What we will do then is

we will dye diesel fuel. Now, that is a great idea. Right? There is only one problem with it.

The pipelines all over this country require that all distillate fuel put in meet diesel fuel specifications. So, now you are going to tax home heating oils; it is not going to be just the farmers. It is going to be those folks in New England—and I am sure you will hear from Senator Moynihan and Senator Bradley and others—that that is a really bad idea.

Senator BOREN. I think we would get some response from them out of that. There is no doubt about that. Thank you very much. Your comments have been helpful to us, and they will be very helpful when we get into markup on Friday.

[The prepared statement of Mr. Columbus appears in the appendix.]

Senator BOREN. I am pleased now to introduce Mr. Don Schieber, another of my agricultural advisers, representing the Oklahoma Wheat Growers Association. We are very pleased that you are here with us today.

STATEMENT OF DON SCHIEBER, PRESIDENT, OKLAHOMA WHEAT GROWERS ASSOCIATION

Mr. SCHIEBER. Thank you, Senator Boren. I really appreciate the opportunity to represent the Oklahoma Wheat Growers and the National Association of Wheat Growers at the same time.

It seems to me that farmers and custom harvesters also haven't been mentioned today, but across the country, if you use substantial amounts of diesel fuel to operate farm machinery this new way of collecting tax will simply provide an interest-free loan to the U.S. Government over a period of several months.

Now, since the first of January of 1986, if my figures are correct, we have lost about 67 banks in the State of Oklahoma alone. There is a numerous amount of farmers now who don't have a bank. So, where are they going to come up with this money, or how are they going to come up with this money if they are now operating out of their billfold because they haven't been able to settle with FDIC?

So, this complicates that procedure also. Farmers, on the other hand, will have to add the anticipated tax outlays to their operating costs, which they are going to have to finance somehow.

It is one thing to raise taxes as a way of reducing the Federal deficit, but it is quite another to collect a tax that is not owed in the first place.

The refund system provided for in the law does allow the farmer to ultimately recover his outlay, but only as the result of additional record-keeping and paperwork. The quarterly refunds will not be possible for a great many farmers to request because of the requirement that a minimum tax of $1,000 be paid in that quarter before a refund can be requested.

Now, this brings up another question. Are we going to have to qualify in each of the four quarters to request the $1,000 refund? Now, seasonal usage of diesel fuel in the farm sector, you may qualify in one quarter or two quarters, but not in all four.

Senator BOREN. Yes, that is a good point.

Mr. SCHIEBER. Even if the farmer did qualify, you know, it is going to be difficult to keep his paperwork up when he is on the combine or on the tractor; it is just going to be a mess.

Agriculture is still struggling to recover from several of the worst years we have seen since the depression; but at the same time, we have been doing our share to close the budget deficit that threatens the stability of the national economy. Commodity spending will decline by over 20 percent this year, compared to last year because of structural changes brought about by the 1985 Farm Bill, which included a phase down of income supports through 1990. The 1987 reconciliation bill further cuts farm income by lowering target prices for both the 1988 and the 1989 green crops by 1.4 percent.

So, the additional burden of paying taxes we don't owe is most unwelcome in the farm community.

The wheat growers support legislation to permit farmers to continue purchasing diesel fuel tax-free for off-highway use, as well as custom harvesters. We are hopeful that the legislation can be enacted as soon as possible since the new collection rule goes into effect in a couple of weeks.

The only recourse farmers presently have is to stockpile diesel fuel supplies between now and April 1. This, of course, is no solution to the problem. We, therefore, ask for your help in expediting the legislation and also in requesting delayed implementation of the rule to allow time for the correct legislation to be put in place. Thank you.

Senator BOREN. Thank you, Mr. Schieber. I agree with your statement, and I think you have made a very good point about this refund problem. We do have seasonal use and swings in usage and so on. So, it would be almost impossible to make a determination as to which people would qualify for quarterly refunds and which would not.

This is a burden that just shouldn't be placed on agriculture right now. I want to thank all of our panel for the contributions you have made.

[The prepared statement of Mr. Schieber appears in the appendix.]

Senator BOREN. As you know, we need to have this hearing record for the full committee so that they will have a factual basis upon which to operate when we do have markup on Friday; and we intend to move very, very quickly on this.

And your willingness to come on short notice and appear at this hearing and help us make this record for the full committee is very much appreciated so that we can move forward with, we hope, unusual speed for Government activity, and to provide some relief.

Your participation in this has been very, very helpful, and I thank all of you very much.

Our last witnesses this morning consist of a panel of three, Mr. Ellis Edwards, who is the Treasurer of the State of Oklahoma, testifying on behalf of various Government organizations that are impacted by this legislation, the Government Finance Officers Association, the National Governors Association, the National League of Cities, the National Associate of State Treasurers, and the National Association of Fleet Administators. I might say that Mr. Edwards in addition to speaking for units of Government that are im-

pacted today, also has shown great sensitivity to the agricultural sector in our State with new investment plans and programs to enable the usage of funds paid by farmers into the State treasury to be used to help provide additional capital for agricultural development. That is something for which he is widely appreciated in our State.

We have Mr. Jerdy Gary with us, who no hails from Denison, Texas, the President of Sooner Oil Company and Former Member of the Board of Directors, Petroleum Marketers Association of America; and of course, he is widely known to all of us in Oklahoma. He has been a local official himself, a mayor, the son of a very distinguished former Governor of the State of Oklahoma—and one of my mentors, Raymond Gary—throughout my political life.

We are also very happy to have with us Mr. Michael Bright, the General Manager of Citgo for Tax of the Citgo Petroleum Corporation.

We are very pleased to have all three of you with us. I will begin with Ellis Edwards.

STATEMENT OF ELLIS EDWARDS, TREASURER, STATE OF OKLAHOMA, TESTIFYING ON BEHALF OF THE GOVERNMENT FINANCE OFFICERS ASSOCIATION, NATIONAL GOVERNORS' ASSOCIATION, NATIONAL LEAGUE OF CITIES, NATIONAL ASSOCIATION OF STATE TREASURERS, NATIONAL ASSOCIATION OF FLEET ADMINISTRATORS, NATIONAL CONFERENCE OF STATE LEGISLATURES, U.S. CONFERENCE OF MAYORS, NATIONAL ASSOCIATION OF COUNTIES, NATIONAL ASSOCIATION OF STATE BUDGET OFFICERS, NATIONAL SCHOOL BOARDS' ASSOCIATION

Mr. EDWARDS. Good morning, Senator. I am here doing yeoman's duty, and I would like to enter my whole statement in the record so as not to take your time up with that statement.

Senator BOREN. We will put the full statements of all three of you into the record.

Mr. EDWARDS. I am here for the National Governors' Association, the National Association of State Treasurers, the U.S. Conference of Mayors, the National League of Cities, the National Association of Counties, the Government Finance Officers Association, the National Association of State Budget Officers, the National Association of Fleet Administrators, National Association of State Legislatures, and the National School Boards Association.

Senator BOREN. I don't know if we have enough hats for you to put on.

Mr. EDWARDS. That is correct. [Laughter.]

And all of those people—or many of those people—or some portion of all of those people—represent everybody that has been here testifying today. It is a burden on the people who have been testifying obviously today, such as the farmers and the boat operators and so forth.

But every one of those people is a citizen of some State. Many of them are citizens of some city or town. All of them are members of a school district all across the United States.

So, not only are they getting hit personally with administrative costs and paying a hidden tax to the Federal Government—and

this is a hidden tax—but they are also getting hit by paying the tax again to those various governmental entities who have to pay the tax because they are the one who support those governmental entities. It is their government as is this Government.

And when their governments—their smaller units of government—have to pay a tax to the Federal Government, the burden is really on them. A minute ago I heard in testimony that, by doing this, we had 300 or 1,000 refiners—I cannot remember the exact figure—that we have to keep records on nationally, instead of the hundreds of thousands or hundreds or several thousands that IRS had to before.

But in fact, there are 83,000 governmental units alone, plus all the farmers and ranchers and small boat operators. So, what we have done is we have created an administrative nightmare, both on the local level and the Federal level.

And it is sort of like saying, it is undoubtedly true that this Government has a national—a major national—drug problem that is a threat to every single American; and if we just passed a law that said nobody could bring a suitcase or a bag or a package in and out of this country, and anybody doing so would be shot, undoubtedly it would reduce the drug traffic.

And that is the kind of solution that has been imposed on the farmers and ranchers and the cities and town in this instance; and it may be more of a problem of enforcement and a need for better enforcement. And it is true that some enforcement may be expensive, but the problem is not just for big cities or big States.

You can imagine the State of Oklahoma pays $771,000 in fuel taxes a year, and they have many different agencies. Some agencies are completely separate, such as mine, elected separately from the people, by the people, than other agencies.

And it is very, very hard and very expensive consequently to coordinate the fuel refund that would be due. The bookkeeping effort would involve, for Oklahoma alone, several hundred thousand dollars. And for Oklahoma City that pays—and I have got those figures—$145,000; they use 1,592,000 gallons of fuel a year and pay $145,000 in taxes. The city of Tulsa uses 1,742,000 gallons of fuel; they must drive more up there, and they pay about $158,000 in taxes.

And then, a little town like Grove uses 16,000 gallons of fuel and pays $9,100 in fuel taxes, and the administrative burden for some of the smaller cities—they may buy their fuel at a local retail store—they are not going to buy it from the wholesaler—and they have a bookkeeper who comes in one time a month. And suddenly, they have got to add another person at a great bookkeeping burden to the State or to their city and they are paying a hidden tax because they are loaning the Federal Government—because of the Federal Government's deficit—money for the whole year.

They can't offset it. These cities and towns can't offset it—and the State Governments can't offset it—against any other tax because they are not taxpayers. They are tax exempt in the first place and ought to remain tax exempt through the whole process.

Senator Nickles' bill would completely address this problem. Several of the bills—Senator Daschle's bill and several other bills—partially address different aspect of the problem; and I would hope

that a number of those legislative acts would be coordinated and maybe meshed into one to address it all.

I hope the cities and towns are not forgotten. I am the one person here testifying for them, but there are a lot of people out there, and they represent every one of the people who were here today. Thank you.

Senator BOREN. Thank you very much. I think that is exactly what we hope to do—that is, have a comprehensive solution—dealing with the gasoline problem, the diesel problem, the gasohol blending problem, so that we take care of all the areas that are being impacted

You make a good point. You were trying to simplify and we are throwing into the mix now 83,000 units of government that have not previously been facing this kind of burden

I know in small towns additional paperwork would cost them $1,000 to $2,000; in some of our smaller communities, it can make a difference between cutbacks in law enforcement or fire protection or other essential services. They simply don't have any other means of obtaining funds, particularly in parts of the country now that are very hard hit.

They have had a decline in their sales tax revenues, and they cannot afford to raise the water bills or utility rates on people who are already in terrible economic trouble. And it is really unfair to put this additional burden on them.

I think you have made a very good case.

Mr. EDWARDS. Thank you, Senator. It really is not just the cities and towns. They are just owned by all of the people who were here testifying who are having this problem and people who aren't even aware they have the problem.

Senator BOREN. Yes, a double impact. Thank you very much. Mr. Gary, we are very glad to have you with us today. It is good to see you again, and we appreciate your taking the time to come up and testify.

[The prepared statement of Mr. Edwards appears in the appendix.]

STATEMENT OF JERDY GARY, PRESIDENT, SOONER OIL CO., AND FORMER MEMBER, BOARD OF DIRECTORS, PETROLEUM MARKETERS ASSOCIATION OF AMERICA, DENISON, TX

Mr. GARY. Thank you, Mr. Chairman. As you indicated, our company, Sooner Oil Company, has been in operation in Denison, Texas for the past 30 years, servicing 35 retail outlets in north Texas and southern Oklahoma. I am a past president of the Texas Oil Marketers Association and a past board member of the Petroleum Marketers Association of America, the PMAA.

I am here today representing the PMAA and the 10,000 small independent petroleum marketers that it represents. Collectively, these marketers account for over half of the motor fuel sold in the United States. Mr. Chairman, PMAA has been working on motor fuel excise tax collection issues for several years now.

My written statement details concerns in both the diesel fuel and gasoline areas. In the interest of time, I am going to focus my oral

remarks on the change in the gasoline excise tax collection procedures.

Under this new procedure, which took effect January 1, 1988, the point of taxation occurs when gasoline leaves the terminal and is loaded at the trucks for further distribution. The seller of gasoline at that point, usually a terminal operator, refinery or importer would collect the tax from the purchaser and remit it to the Internal Revenue Service on a specified payment schedule. In many ways, this new procedure improved the collection of gasoline excise taxes and reduced significantly the incidence of excise tax evasion.

It did this by defining clearly a point of taxation for gasoline. However, there are at least three problems with the new system which need to be addressed as soon as possible.

Previously, as an independent marketer, I enjoyed the same rights as refiners in terms of remitting the Federal excise taxes on gasoline. This is an important change because in the petroleum industry, refiners, suppliers often compete directly with their independent marketers for business.

By requiring that independent marketers pay their excise tax directly to the supplier, rather than to the Federal Government, it gives that refiner/supplier a competitive advantage over the independent marketer.

For example, if I purchase a load of gasoline today, I must pay for it, including all the excise taxes, by March 26. The refiner, however, under the IRS payment schedule does not have to remit my tax dollars to the Government until April 9. Moreover, if my refiner competes with me, he can take a load of gasoline today to his direct operated outlets, sell it in a two or three day period, and not remit the taxes for over three weeks. I can tell you in my own situation that we lose approximately $67,000 a month in cash flow to our suppliers.

The second problem which needs to be addressed concerns the ability of State and local governments to buy gasoline tax-free. The Internal Revenue Code allows State and local governments to buy tax-free if the taxpayer will agree to apply for the refund directly.

Unfortunately, wholesale distributors like myself are no longer considered taxpayers. Therefore the only way we can sell tax-free to a State or local government is if our supplier is willing to refund the money directly to us.

The third problem relates to gasohol. There are indications within IRS that when final excise gasoline tax regulations are issued, gasohol blenders who buy gasoline and ethanol at separate terminals will no longer be entitled to the reduced tax rate.

Since few terminals supply both gasoline and ethanol, those marketers are forced to buy at separate terminals are placed at a competitive disadvantage versus those marketers who have the luxury of buying both products at the same terminal.

PMAA believes that each of these problems can be remedied by a very simple amendment. This amendment would allow purchasers of gasoline at the terminal to remit the Federal excise tax directly to IRS provided the purchaser is registered as a tax remitter and agrees to comply with any bonding or financial responsibility requirements imposed.

There are several advantages to this amendment. First, it would correct the competitive advantage refiners have over marketers by giving marketers the right to remit the tax directly to the IRS based on their purchases from the refiner.

Second, it would allow those State and local governments supplied by the local marketers to purchase tax-free.

Third, by allowing wholesale purchasers at the terminal to remit the tax, gasohol blenders would be able to pay the reduced tax rate to IRS directly on those gallons that are blended.

Finally, the change would still provide IRS a clear-cut audit trail to prevent tax evasion. IRS can merely match a wholesale distributor's purchases at the terminal with the taxes that he remits. In addition, there should not be any new taxpayers under this system since all the eligible marketers already remit diesel fuel excise taxes and are thus already subject to IRS enforcement procedures.

I would urge this committee to act as expeditiously as possible in approving this amendment, along with the recommended changes we have described in our written testimony relative to diesel fuel. The PMAA strongly supports Congressional efforts to end excise tax evasion; however we believe that the simultaneous goals of ending evasion and creating an equitable marketplace can be achieved by adoption of the proposals we have outlined.

Thank you very much.

Senator BOREN. Thank you very much. I think you make an important point that has not been made up to this time about the changes of competitive balance within the industry that occur when you change the point of collection. I think that is an important matter for us to consider, and I appreciate your bringing that out and explaining it for the record—how that occurs.

We appreciate your testimony very much.

Mr. GARY. Thank you. Mr. Chairman, if I could make one comment in that regard? I just learned this morning that in Texas one of my colleagues lost a major municipality to his supplier, strictly on this problem that I just outlined here in my testimony.

Senator BOREN. Right. I can certainly see why it happens, and it is going to become more widespread if this is not changed.

[The prepared statement of Mr. Gary appears in the appendix.]

Senator BOREN. Mr. Bright, we are happy to have you with us as our last witness today, but certainly not least important by any means; and I appreciate your patience in being with us through the morning and remaining with us to conclude our testimony. We look forward to hearing your statement.

STATEMENT OF R. MICHAEL BRIGHT, GENERAL MANAGER, TAX, CITGO PETROLEUM CORP., TULSA, OK

Mr. BRIGHT. I am Mike Bright, and I am General Manager of Taxes for Citgo. Citgo is based in Tulsa, Oklahoma and is a refiner/marketer of crude oil, gasoline, lubricants, and distillates in the United States.

In my position with Citgo, I am essentially involved in the compliance function of the motor fuel excise taxes. My testimony today will deal with the problems of the gasoline taxes; however, I am also submitting written comments on the diesel fuel taxes.

Senator BOREN. We will receive your full comments for the record.

Mr. BRIGHT. I will try to answer the question that you previously asked the IRS about the statutes and so forth on the gasoline taxes. The statutes were changed by the Internal Revenue Code of 1986, which was passed in October of 1986, to take effect on January 1, 1988.

However the IRS did not issue any form of proposed regulations or other information to the public until November 18, 1987. Then they scheduled a hearing on January 5, 1988 which was five days after the law took effect.

In February 1988, we received the final regulations from the IRS. It was obvious from the hearing on January 5 that the IRS did not understand the petroleum industry which it was trying to tax nor the transactions that transpire in this industry.

Despite these changes, there were several improvements in the February regulations; but there are still two or three items that we need to consider. One is the same terminal rule for the blending of gasohol. Gasohol is a blend of gasoline and alcohol, and under the final regulations that the IRS published in February 1988, gasohol will have to blended at the same terminal as of April 1.

However, on March 14, they extended that date to June 30. So, we are still going through changes in the gasoline regulations.

Alcohol plants require a large capital investment, and they cannot economically be moved to a gasoline terminal. Laying pipelines and so forth through residential areas also increase environmental problems. We need to consider eliminating that part of the gasoline bill.

The other thing is the bonding requirement. Congress has passed two instances where taxpayers must be bonded in order to collect the Federal excise tax, one to deal with the diesel fuel tax and one to deal with the gasoline tax. Both of these instances deal with the oil industry, which gives us a public image of being untrustworthy and uncreditworthy.

However, at the same time, the IRS states they are requiring us to collect the taxes because we are more financially stable than the other taxpayers. We believe this is totally unfair, and we think it is very dangerous because the next step will be to require bonding of payroll tax collectors.

The petroleum industry—or Citgo—if given ample time, can deal with the regulations that you propose. We need a concerted effort by Congress, Treasury, and industry to implement the intent and achieve your desires in these regulations.

Citgo fully recognizes and accepts its responsibility for collecting and remitting in a timely fashion the proper amount of gasoline excise tax. We understand and support Congress' intent to institute stronger measures to ensure complete accountability and compliance.

However, implementation of Congressional intent with respect to gasoline tax has been chaotic and disruptive. Despite the lack of regulatory direction, the industry has struggled to interpret the law and implement it. Because of the disastrous way in which the regulations were promulgated, we at Citgo do not believe penalties should be imposed for varying tax collection processes considering

the industry's good faith and their efforts during this time of confusion.

We believe that, until concise and clear and consistent regulations are implemented penalties are not in order.

A comment on the diesel fuel tax. The proposed bills that have come out made a fifth category, the farmer. You need to understand that several farmers in Oklahoma and several tax exempt organizations in Oklahoma have to buy their gasoline or diesel fuel from their retail seller. We need to be sure that we put something in the regulations or in the law that allows that to happen on a tax-free basis.

I have to comment, before I can go back to Oklahoma, about a small community in Oklahoma where I am from that doesn't have a wholesale distributor available to the schools, and this is a severe hardship upon that community.

Thank you very much for allowing us to testify.

Senator BOREN. Thank you very much, Mr. Bright.

[The prepared statement of Mr. Bright appears in the appendix.]

Senator BOREN. I appreciate all of you being here today. We wanted to listen to all the aspects of the communities and businesses in our country that have been impacted by this. We have heard you. We understand the problem. We think it is a real problem; a serious mistake has been made here. Undue burdens have been put on sectors of this economy that can least afford to bear those burdens.

Usually you tax people on the ability to pay. This seems to be a tax burden that has been placed on those who are absolutely unable to bear the burden and have no way of passing this burden on; and it is something that simply ought to be changed. So, it is my hope that we are going to set a few records around here in trying to get this reversed and do it with enough speed that we can avoid the impact before it hits us.

Again, I want to thank all of you who have been a part of this today. We will keep the hearing record open for additional statements that we have received, and we have received indications that others want to submit statements.

There are also some questions that some of the members may want to ask for the record, particularly of the IRS; and we will leave the record open also for that purpose.

[Whereupon, the hearing was concluded.]

[By direction of the chairman the following communications were made a part of the hearing record:]

APPENDIX

ALPHABETICAL LIST AND MATERIAL SUBMITTED

COLLECTION PROCEDURES FOR EXCISE TAXES

ON GASOLINE, DIESEL, AND NONGASOLINE AVIATION FUELS

(S. 2075, S. 2003, S. 2062, S. 2067, S. 2118, AND S. 2128)

Prepared by the Staff

of the

JOINT COMMITTEE ON TAXATION

JCX-3-88

March 15, 1988

INTRODUCTION

The Subcommittee on Energy and Agricultural Taxation of the Senate Committee on Finance has scheduled a public hearing on March 16, 1988, on collection procedures and exemptions for excise taxes on gasoline, diesel, and nongasoline aviation fuels. This document,[1] prepared by the Staff of the Joint Committee on Taxation, provides a description of present law and legislative proposals relating to such motor fuel tax collection procedures and exemptions.

The first part of the document is a summary. The second part is a description of present-law collection procedures and exemptions, and of the provisions of six Senate bills: (1) S. 2075 (introduced by Senators Daschle, Armstrong, Baucus, Boren, Danforth, Durenberger, Pryor, Roth, Riegle, and others); (2) S. 2003 (introduced by Senators Gramm, Durenberger, Wallop, Armstrong, and others); (3) S. 2062 (introduced by Senator Nickles and others); (4) S. 2067 (introduced by Senator Conrad and others); (5) S. 2118 (introduced by Senator Gramm); and (6) S. 2128 (introduced by Senators Warner, Chafee, Mitchell, and others).

I. SUMMARY

Gasoline excise tax

The gasoline excise tax is imposed on removal of gasoline blend stocks from the refinery or from a bonded terminal to which the blend stocks are transferred in bulk. In general, all exemptions for specified uses of gasoline are realized by means of refunds following tax-paid sales.

Diesel and nongasoline aviation fuels excise taxes

Effective after March 31, 1988, the excise taxes on diesel fuel and nongasoline aviation fuels are imposed on the sale of the taxable fuel by a producer, defined to include wholesale distributors as well as actual producers of the fuels. Most exemptions from these taxes are realized by means of refunds following tax-paid sales. Special rules are provided allowing sales without payment of tax in the case of trains, commercial airlines, feedstock use, and use by States and local governments. These special rules require that purchasers register with the Internal Revenue Service and provide proof of financial responsibility.

Before April 1, 1988, these excise taxes are imposed on the retail sale of the taxable product and exemptions generally are realized by means of tax-free sales.

Overview of the bills

Gasoline excise tax

Certain of the bills would permit sales of gasoline without payment of tax where the gasoline was to be used on a farm for farming purposes. Additionally, under one bill, wholesale distributors would be permitted to remit the gasoline tax (instead of refiners or terminal operators as under present law).

Diesel and nongasoline aviation fuels excise taxes

The bills would restore the ability of some or all of the persons who under the law before April 1, 1988, may purchase diesel fuel without payment of tax for use in an exempt use to continue to do so, in some cases subject to registration and financial responsibility requirements.

II. PRESENT LAW AND PROPOSALS RELATING TO COLLECTION OF EXCISE TAXES ON GASOLINE, DIESEL, AND NONGASOLINE AVIATION FUELS

A. Present Law

1. Gasoline excise tax

Imposition of tax

An excise tax of 9.1 cents per gallon is imposed on removal from the refinery (customs custody for imported gasoline) or sale (if earlier) of gasoline, gasoline blend stocks, and products commonly used as additives in gasoline (Code sec. 4081). An exception is provided permitting bulk transfers of gasoline, gasoline blend stocks, or additives to registered and bonded terminals without payment of the tax. In such cases, terminal operators are liable for collection and payment of tax upon removal of the taxable fuel from the terminal. Revenues equivalent to this tax are deposited in the Highway Trust Fund (9 cents per gallon)[2] and the Leaking Underground Storage Tank Trust Fund (0.1 cent per gallon).[3]

Before January 1, 1988, the gasoline excise tax was imposed on the sale of gasoline by a "producer", which was defined to include wholesale distributors and other intermediaries (other than retailers) in the chain of gasoline distribution who registered with the Internal Revenue Service.

The current gasoline tax payment procedures were enacted by the Tax Reform Act of 1986, effective on and after January 1, 1988.

Gasoline mixed with alcohol ("gasohol")

Registered gasohol[4] blenders are permitted to purchase gasoline under present law at a 3.1 cents-per-gallon tax on the gasoline component of the mixture,[5] if blending occurs at the terminal. In all other cases, gasohol blenders (like other purchasers) must purchase gasoline and gasoline blend stocks tax-paid (at the full 9.1 cents per gallon). However, they may claim a refund of any tax paid on purchases to the extent that excess tax is paid.

A special, accelerated refund procedure is provided for gasohol blenders who buy gasoline tax-paid. Under this procedure, refund claims may be filed weekly, and if the Treasury Department has not paid a claim within 20 days of the date of filing, the claim is to be paid with interest from such date.

Registration and bond

Every person subject to the gasoline excise tax who receives non-tax-paid gasoline is required to register with the Treasury Department and may be required, under Treasury regulations, to post bond in such amount as the Secretary determines (sec. 4101).

Exemptions

Farmers.--If gasoline is used on a farm for farming purposes, farmers may claim an income tax credit for tax paid on the gasoline (sec. 6420).

State and local governments, nonprofit educational organizations, and buses.--State and local governments and nonprofit educational organizations must purchase gasoline tax-paid and apply for a full refund of the tax (sec. 6421(c)). If a refund of $1,000 or more of gasoline tax is due with respect to gasoline used during any of the first three quarters of the taxable year, a claim for refund may be filed for tax paid in that quarter. Otherwise, only one refund claim per taxable year may be filed. These refund procedures also apply with respect to gasoline purchased (tax-paid) for use in State and local buses, school buses, and intercity or local buses (sec. 6421(b)).

In general, only an exempt user may file a claim for refund; however, under a special procedure, sellers may, in certain cases file the claim on behalf of the exempt user (sec. 6416). Thus, in the case of sales to States and local governments, for use in vessels, and certain other uses, if a seller demonstrates that the exempt user is billed for a price "net of tax," the seller may claim the refund.

Exports and supplies for vessels.--Gasoline for export or for use as supplies for vessels is no longer tax-free when sold but is subject to the same refund or credit rules as for State and local governments, nonprofit educational organizations, and buses.

Other non-highway users.--Taxpayers other than governmental units or tax-exempt organizations who use gasoline in off-highway business uses also must purchase gasoline tax-paid and realize their exemptions by means of an income tax credit or refund. Generally, these users may only claim a credit on their income tax returns (secs. 34 and 6421(i)), unless they meet the $1,000 per quarter rule, described above, for refunds (sec. 6421(d)(2)).

2. Diesel and nongasoline aviation fuels excise taxes

Post-March 31, 1988

Effective after March 31, 1988, the excise taxes on diesel fuel and nongasoline aviation fuels ("jet fuel") will be imposed on the sale of those fuels by a producer, or use of the fuels if before payment of tax otherwise is made (sec. 4091). The term producer is defined to include wholesale distributors as well as refiners and certain other intermediate persons (other than retailers) in the chain of distribution of these fuels. All producers of taxable fuels must register with the Treasury Department and satisfy such bonding requirements as Treasury prescribes.

Exemptions from these taxes are provided for several specified uses. In the case of diesel fuel, exemptions are provided for, inter alia--

(1) Use exclusively by States and local governments;

(2) Use on a farm for farming purposes;

(3) Use by an educational organization exempt from income tax under Code section 501(c)(3);

(4) Use by certain aircraft museums; and

(5) Use other than as a fuel in a highway vehicle.

The tax on nongasoline aviation fuel applies only to such fuels used in noncommercial (general) aviation, defined as aircraft use other than the carrying of passengers or freight for hire.

Effective on and after April 1, 1988, most exemptions from these taxes will be realized through refunds. Thus, tax generally will be imposed on all sales with the ultimate user of fuel used for an exempt purpose claiming a refund from the Treasury Department. These refunds may be claimed in either of two ways. First, a credit against the user's income tax is permitted (sec. 34). Second, a person entitled to a refund of $1,000 or more during any one of the first three calendar quarters of a year may file a claim for refund of tax paid during that quarter (sec. 6427). Third, States and nonprofit users may file claims for refund annually without regard to the amount of tax for which the claim is made (or quarterly subject to the $1,000 threshold).

The Treasury Department is authorized to establish procedures for permitting sales without payment of tax, on a case-by-case basis, for certain uses where the purchaser demonstrates to Treasury's satisfaction that the fuel will be used in a nontaxable use and also registers and satisfies such financial responsibility requirements as Treasury may require. Sales that are exempt from tax include only direct sales by a producer to an ultimate user for exempt use. These sales are permitted only in the case of (1) diesel fuel sold for use as fuel in a diesel-powered train; (2) aviation fuel sold for use as fuel in an aircraft in commercial aviation; (3) taxable fuels sold for industrial use other than as a motor fuel (i.e., as a chemical feedstock); and (4) taxable fuels sold for exclusive use of any State or local government. An additional exemption permits diesel fuel that Treasury determines is destined for use as heating oil to be sold without payment of tax.

These provisions were adopted as part of the Omnibus Budget Reconciliation Act of 1987.

Pre-April 1, 1988

Before April 1, 1988, the excise taxes on diesel fuel and nongasoline aviation fuels are imposed on the retail sale (or earlier taxable use) of these fuels. In general, exemptions from these taxes are realized through tax-free sales, rather than through refunds or credits.

B. Description of Bills

1. S. 2075 (Senators Daschle, Armstrong, Baucus, Boren, Danforth, Durenberger, Pryor, Roth, Riegle, and others)

S. 2075 would provide that the present-law direction to the Treasury Department to issue regulations allowing sales of diesel and nongasoline aviation fuels without payment of tax in certain cases is mandatory and that those regulations must be issued no later than 30 days after the date of the bill's enactment.

The bill further would permit sales of diesel fuel without payment of tax for use on farms for farming purposes subject to the same conditions as those under present law for States and local governments. Thus, bulk sales for this purpose made directly by producers to the farm users would be exempt when the purchaser had registered and satisfied Treasury financial responsibility standards.

Effective date

The bill would be effective for sales of taxable fuels occurring after March 31, 1988. A special refund procedure would be provided for any exempt users who paid tax on these fuels before the mandated Treasury regulations were issued.

2. S. 2003 (Senators Gramm, Armstrong, Durenberger, Wallop, and others)

S. 2003 would provide that sales of diesel fuel for use on a farm for farming purposes would be tax-free. These tax-free sales would be available without regard to any Treasury discretion or mandatory registration and financial responsibility requirements. In addition to direct sales to farm users, sales by wholesalers to retail dealers who resell the gasoline to State or local governments would be made without payment of tax.

Effective date

The bill would be effective for sales of taxable fuels occurring after March 31, 1988.

3. S. 2062 (Senator Nickles and others)

S. 2062 would direct the Treasury Department to adopt regulations permitting States and local governments to purchase gasoline without payment of tax. In addition to direct sales where these governments purchase fuel from the refinery or a pipeline terminal, sales to wholesale distributors who resell the gasoline to States or local governments would be made without payment of tax.

Effective date

The bill would be effective upon enactment.

4. S. 2067 (Senator Conrad and others)

Sales of diesel fuel for farm use

S. 2067 would permit sales of diesel fuel without payment of tax for use on farms for farming purposes subject to the same conditions as those under present law for States and local governments, except sales to intermediate parties such as retail dealers for resale to farms also would be made without payment of tax.

Wholesale gasoline distributors

The bill would permit wholesale distributors to remit the excise tax on gasoline, subject to satisfaction by such dealers of such registration and financial responsibility requirements as the Treasury Department adopts. (The bill would not change the taxable event for the gasoline tax or the timing of payments of that tax.)

Wholesale distributor would be defined to mean any person who (1) sells gasoline to retailers or to users who purchase in bulk quantities and deliver into bulk storage tanks, or (2) purchases gasoline from a person who would pay the tax under present law, i.e., any producer or importer of gasoline, and distributes such gasoline to 10 or more retail gasoline stations under common management with such person.

Gasoline sales to farmers and gasohol blenders

The Treasury Department would be directed to permit sales of gasoline without payment of tax for use on a farm for farming purposes, both in the case of direct sales from the refinery or pipeline terminal to a farmer and in the case of sales to wholesale distributors who re-sell the gasoline for farm use. Persons purchasing gasoline without payment of tax would be required to register with Treasury and to satisfy such financial responsibility requirements as Treasury might require.

The partial exemption from the gasoline tax (9.1 cents per gallon) for gasoline used in producing a gasohol blend at the time of the sale or removal would be extended to apply to gasoline sold to produce a gasohol blend after the time of the sale or removal. The Secretary would be given authority to prescribe the terms and conditions necessary to carry out this amendment.

Effective dates

The provisions of the bill generally would be effective upon enactment. The provision relating to diesel fuel sold for farming use would apply to sales occurring after March 31, 1988.

5. S. 2118 (Senator Gramm)

The Treasury Department would be directed to prescribe regulations under which no tax on diesel fuel would be imposed on sales for use by the purchaser in an off-highway use, or for resale by the purchaser to a second purchaser for use by the second purchaser in such a use.

The term off-highway use would be defined as any use not as a fuel in a diesel-powered highway vehicle or a diesel-powered train.

Effective date

The bill would be effective for sales occurring after March 31, 1988.

6. S. 2128 (Senators Warner, Chafee, Mitchell, and others)

S. 2128 would permit sales of diesel fuel without payment of tax for use in fishery vessels subject to the same conditions as those under present law for sales without payment of tax to States and local governments, except sales to other intermediate parties (e.g., retail dealers) who stated that the fuel ultimately would be used in a fishery vessel also would be made without payment of tax.

A fishery vessel would be defined as a fish harvesting vessel, a fish tender vessel, or a fish processing vessel.

Effective date

The bill would be effective for sales occurring after March 31, 1988.

FOOTNOTES

[1] This document may be cited as follows: Joint Committee on Taxation, Collection Procedures for Excise Taxes on Gasoline and Diesel and Nongasoline Aviation Fuels (S. 2075, S. 2003, S. 2062, S. 2067, S. 2118, and S. 2128) (JCX-3-88), March 15, 1988.

[2] The "Highway Trust Fund financing rate" is scheduled to expire after September 30, 1993.

[3] The "Leaking Underground Storage Tank Trust Fund financing rate" is scheduled to expire after the earlier of (1) December 31, 1991, or (2) the end of the month for which Treasury estimates that this Trust Fund's net tax revenues (net of refunds and credits) reach $500 million.

[4] "Gasohol" is any mixture of gasoline if at least 10 percent of the mixture is alcohol with a proof of 190 or more. Alcohol includes methanol and ethanol, but does not include alcohol produced from petroleum, natural gas, or coal.

[5] Gasohol is eligible for a 6-cents-per-gallon exemption from the 9-cents-per-gallon Highway Trust Fund financing tax rate.

STATEMENT OF SENATOR DAVID BOREN

I have called this hearing today to discuss the collection of federal gasoline and diesel fuel excise taxes. There has been a great deal of concern over the past several months concerning changes in the collection of these taxes. These changes were the result of the Tax Reform Act of 1986 and the Omnibus Reconciliation Act of 1987.

Gasoline Tax Collection:

An excise tax of 9.1 cents is imposed on the sale of gasoline for use in a highway vehicle. The Tax Reform Act of 1986 moved the collection point of the gas tax from sales at the wholesale level to removal of the fuel from the terminal. When the gasoline is removed from the terminal and loaded into a truck for distribution, the terminal operator is generally responsible for collecting the tax from the purchaser and remitting the tax within 2 to 3 weeks.

There appear to be a couple of problems with the current collection system. First, the changes made in the Tax Reform Act of 1986 result in no downstream tax exempt sales, for example to state and local governments. Currently, under Sec. 6416 of the Internal Revenue Code, state and local governments can buy tax free if their vendor is willing to obtain the refund directly. Unfortunately, only "taxpayers" are eligible for this refund. Wholesale distributors and jobbers are no longer considered taxpayers and must depend on the refiner-supplier to refund to them the taxes paid but not collected from the state and local government entity. It appears that some refiners have not indicated a willingness to honor this procedure. Consequently state and local governments served by wholesalers will probably not be able to take advantage of Sec. 6416 and must pay the tax upfront and then file for a refund. This could potentially result in over 83,000 governmental entities being forced to pay the taxes upfront, maintain purchase records and then file for a refund. It would appear the Tax Reform Act of 1986 may have created more of a problem than it solved.

Diesel Excise Tax Collection Process: PMAA Solution

IRS is not the only problem relative to the change in diesel fuel collection procedure. There are some obvious problems which will require statutory correction. The most obvious of these problems is the requirement that farmers, marinas, and drilling contractors, and other off-road users must pay the tax directly to the wholesaler distributor or refiner.

This creates two tremendous problems. First, it means a tremendous loss of cash flow to the farmer and other off-road users. The American Farm Bureau estimates that American farmers would be paying $420 million per year to their suppliers, who would turn that money over to the IRS which would then either refund the money or provide a credit on the farmers' income tax return. This would be another devastating blow to America's agricultural community.

The second problem relates to suppliers of diesel fuel to the farmer. The supplier is, in most cases, a wholesale distributor. By necessity, these distributors often offer liberal credit terms to their agricultural accounts. In some instances, the fuel bill is not paid until the crop is harvested. Credit terms to farmers of 60 or 90 days are not unusual. This means these small wholesale distributors will have a substantial increase in their accounts receivable, thus damaging significantly their cash flow. It also could mean higher losses to bad debts if farmers are unable to pay their bills.

PMAA's proposed solution to this problem is simple. We support an amendment which would allow off-road users of diesel fuel to continue to buy diesel fuel minus the tax. This would include farmers, fishermen, marinas, drilling contractors, and others. Adoption of this amendment would be advantageous in that there is no justification to require these users to pay a tax they do not owe and then have IRS refund the money through a cumbersome, bureaucratic procedure.

Nineteen bills have been introduced in the House and Senate between the time the second session convened on January 25 and March 10 which address some aspect of the gasoline and diesel fuel excise tax problem. These bills are summarized as Attachment III.

I am also concerned about a similar problem with the collection procedure for the excise taxes on gasohol. Gasohol, which is a 90/10 blend of gasoline and fuel ethanol, is subject to a 3 cent per gallon Federal excise tax. I am concerned that under the revised gasoline tax collection procedures, many gasohol blenders may be forced to pay three times the lawful tax due when they purchase gasoline to be blended with ethanol. They would then be forced to file for a refund of the overpaid taxes. I would hope that when we solve the problems presented today that we consider the gasohol problem and design a collection system that insures gasohol blenders pay the proper rate of taxes at the outset.

Diesel Fuel Excise Tax Collection:

An excise tax of 15.1 cents per gallon is imposed on the sale of diesel fuel for use in vehicles. Since the diesel tax was originally enacted as a means of financing the federal highway system, most off-highway uses of diesel fuel, such as farm vehicles, drilling equipment, fishing vessels, construction equipment, and barges are exempt from the tax. The Omnibus Reconciliation Act of 1987 moved the collection point of diesel fuel from the retail level to the wholesale level. This change will go into effect in 15 days on April 1st.

Thus the 1987 Act requires diesel fuel taxes to be paid when the fuel is sold by a wholesale distributor to a retail purchaser. Now off-highway users may no longer purchase the fuel tax-free. Instead, most exempt users will have to buy the fuel with the tax already paid and then file for a refund.

Consequently, every farmer who buys diesel fuel for his tractors and other off-highway farm equipment will have to pay an extra 15 cents per gallon and then wait for a refund. That amounts to over $400 million that will be taken out of the hands of farmers for periods raninging up to one full year. This is no way to help a devestated farm economy.

This is not a small problem isolated within a few industries. We will hear today from representatives of the agriculture, oil and gas, coal, and petroleum marketing industries. Time constraints do not allow us today to hear from all industries effected such as construction, commercial fishing, rural electric co-ops, and the barge and towing industry. But that does not mean that this problem is any less significant to those groups. For example, the U.S. barge and towing industry would suffer as a result of this provision because towboat and barge operators, in addition to the inland waterway fuel tax they have been paying since 1980, would also be required to pay the 15 cent per gallon highway tax when purchasing diesel fuel. This is a staggering cash flow burden for an industry that plays a major role in the movement of bulk commodities, domestically and for our export markets. At the Port of Catoosa, in Tulsa, Oklahoma, 1.8 million tons of primarily agricultural and petroleum products were moved in 1987. In the case of inland waterway users, it is competitively unfair to require that fuel used in waterway transportation be subject to the tax while rail and commercial aviation were exempted from this requirement.

The impact of these changes on farmers and state and local governments is tremendous and in my mind wholly unwarranted. I simply do not believe we should attempt to reduce the deficit by requiring people to pay a tax they do not owe so that the government can have the use of their money for a period of time. I remain committed to resolving these problems as quickly as possible and I commend the Chairman of the Finance Committee for scheduling a mark-up this Friday.

TESTIMONY OF
MIKE BRIGHT
ON BEHALF OF CITGO PETROLEUM CORPORATION
ON
IMPLEMENTATION OF THE GASOLINE EXCISE TAX

BEFORE THE
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
COMMITTEE ON FINANCE
U.S. SENATE

MARCH 16, 1988

I am Mike Bright, General Manager of Taxes for CITGO Petroleum Corporation. CITGO is based in Tulsa, Oklahoma, and is a refiner and marketer of crude oil, gasoline, lubricants and distillates in the United States. I am a graduate of Oklahoma State University, am a Certified Public Accountant, and have worked for fifteen years in various tax positions with CITGO and its predecessors. I am intensively involved in CITGO's efforts to comply with recent statutory and regulatory changes to the excise tax on gasoline. My testimony before you today addresses those efforts and the remaining compliance problems that we face.

The statutory changes to the gasoline excise tax occur in sections 4081-4083, 4101, 6421, and 6427 of the Internal Revenue Code of 1986. These changes were enacted in the Tax Reform Act of October, 1986. The regulatory provisions implementing the statutory changes were addressed in Notice 88-16 of Internal Revenue Bulletin 1988-7. The statutory changes require that, beginning January 1, 1988, the gasoline excise tax on any taxable sale of gasoline be collected by the producer or importer. These provisions revise the previous collection system, under which the excise tax was collected on the retail sale of the fuel. These provisions now require volumetric accounting of the fuel from the time it is produced or imported to the end-user.

It was not until November, 1987 that the Internal Revenue Service published its proposed regulations to implement the gasoline tax changes. And it was not until January 5, 1988, five days after the new law took effect, that the IRS held a public hearing on the proposed regulations. The proposed regulations

and the testimony in response to them at the public hearing demonstrated clearly that the IRS did not understand the petroleum industry or how the tax was to be collected. The proposed regulations left the entire petroleum industry in a state of confusion and resulted in multiple interpretations in determining what the IRS was trying to achieve. The regulations as proposed would have been extremely onerous and expensive to administer, and would have imposed unnecessary and costly reporting responsibilities on us and our customers. Many small exempt customers would have been exposed to severe financial pressure because they would have been required to pay the tax, file for a refund and wait for the bureaucracy to process the refund request. Moreover, these customers would have faced this process month after month.

It was only after several meetings with industry participants and after several members of the Senate, including two members of this subcommittee, expressed concern to the IRS that the IRS promulgated revised, more reasonable regulations.

The final regulations, which were issued less than a month ago, on February 18, included revisions to several provisions of the proposed regulations that had given CITGO great concern. For instance, the proposed regulations had imposed a blanket requirement that all petroleum industry participants collecting the gasoline tax acquire a bond sufficient to cover expected tax collections for a three-month period. This would have required CITGO to acquire a bond for $100 million, an amount that none of the industry bonding companies were willing to cover. The final regulations significantly modified this requirement to provide that those entities with a satisfactory tax filing and payment history are not required to acquire a bond. While CITGO continues to have concerns about the bond requirement, as I will explain later, we believe this change is a significant improvement. Another helpful change was the redefinition of "bulk transfers" to include marine or pipeline transfers, so that the tax will not be required to be collected at the point of such transfers. Sim-

ilarly, the final regulations provided that the tax is not required to be collected at the point of mere exchanges between registered parties. One further IRS accommodation that CITGO supported was implementation of a set of procedures by which state and local governments, which are exempt from payment of the tax, are able to buy gasoline without having to first pay the tax and then seek a refund.

Despite these changes, there remain several major facets of implementation that are of great concern to CITGO. First, CITGO opposes the imposition of a bond requirement. Congress authorized IRS to require taxpayers to post bonds, but to do so is an implicit indictment of untrustworthiness. CITGO believes imposing the requirement on businesses that are collecting these taxes for the government both establishes a dangerous precedent which could be extended to collection agents of other taxes, and yet without applying it to other collection agents, singles out the petroleum industry as untrustworthy. In no other area of tax collection does the government require bonds, even if only for those entities that are unable to demonstrate a satisfactory tax filing and payment history. There have been four or five instances of failure to submit collected gasoline taxes to the Treasury. Most of these violations were fly-by-night operations; one was a mere paper entity. CITGO does not condone such scofflaws, but we do not believe the entire petroleum industry should be subjected to a costly burden devised to eliminate abuses by such an unethical few.

Businesses are collecting billions of dollars a year for the government in the form of payroll taxes, just to mention one example. And yet despite the vast amounts of tax funds involved, and the many published instances of failure to remit the collected payroll taxes, no bond is required, regardless of the business' previous record of tax filing and payment.

CITGO paid $87 million in taxes to the United States government during 1987. These taxes were all paid on a timely basis and in compliance with the tax law. We believe, therefore, that

our tax filing and payment history is satisfactory, and that we should not be required to post a bond. However, since our District Director has not yet received the necessary procedural guidance from Washington, we have not been issued a gasoline certificate of registry, and do not know with any certainty that we will be allowed to collect these excise taxes without a bond. During the last two years the IRS has misapplied several of CITGO's tax deposits. The problem was the result of internal IRS administrative errors. However, if these misapplications are held by IRS to be the fault of the taxpayer, CITGO could be required to post a bond. The requirement in this case would be an inequitable and unjust expenditure. This situation highlights the need for guidelines regarding what constitutes a satisfactory filing, deposit and payment history. Such standard guidelines are necessary not only to address situations such as this, but also to avoid varying interpretations of the bond requirement and inconsistent application among the different tax districts.

Another unjust aspect of the bond requirement pertains to newly created businesses. New businesses do not have a filing and payment history with the IRS, and the regulations therefore state that they will be required to post a bond. CITGO suggests that if a newly formed corporation is a member of a group of commonly controlled corporations (as defined in section 1504(a)(1) and (2) of the Internal Revenue Code of 1986) whose parent has a satisfactory filing and payment history, there should be no bond requirement. In other words, there should be some procedure under which the parent corporation's history can provide adequate security to the District Director to waive the bond requirements for all members of the controlled group of corporations.

CITGO's second major concern pertains to the regulation's treatment of gasohol -- blends of alcohol and gasoline. Gasohol is eligible for a reduced gasoline excise tax rate. However, the regulations require that in order to qualify for this reduced rate, both the alcohol and the gasoline must be located and blended together at the same product terminal. If the gasoline

and alcohol are purchased from separate terminals and later blended, the gasoline purchased separately will not be eligible for the reduced tax rate. IRS has issued a temporary reprieve from this regulation until April 1, 1988. On March 14, IRS announced that it will extend the reprieve through June 30.

CITGO does not have alcohol blending facilities, therefore this requirement, if not made permanent, will force us to sell our gasoline to blenders at the higher non-gasohol tax rate. The blender must then file for a refund of the tax paid in excess of the gasohol rate, losing significant cash flow during the process. Typically alcohol and gasoline supplies have been located in separate terminals. These terminals are large fixed asset investments which cannot be relocated readily. The "same-terminal" blending requirement therefore is both impractical and extremely uneconomical for most gasohol producers. It will subject CITGO and its gasohol distributor customers to a competitive disadvantage vis-a-vis those suppliers who have access to "same-terminal" supplies. CITGO believes the "same-terminal" requirement should be eliminated.

A third point we would like to make with respect to the gasoline tax regulations is the need to give the industry ample time to implement the changes in the law. Currently, neither the district offices nor the taxpayers can meet the demands placed on them by the changes in these regulations. Given ample time, and with a concerted effort from Congress, Treasury, and industry, there is no doubt that we could implement this legislation and achieve the goals Congress intended. CITGO fully recognizes and accepts its responsibility for collecting and remitting in a timely fashion the proper amount of gasoline excise tax. We understand Congress' intent to institute stronger measures to insure complete accountability and compliance. However, implementation of congressional intent with respect to the gasoline tax has been chaotic and disruptive. Despite the lack of regulatory direction, the industry has struggled to interpret the law and implement it. Because of the disastrous way in which these

regulations were promulgated, we at CITGO do not believe penalties should be imposed for varying tax collection practices among industry participants in their good faith efforts to interpret and comply with the law. We believe that until concise, clear and consistent regulations are implemented, penalties are not in order.

Gasoline demand in the United States in 1987 was 2.6 billion barrels. CITGO satisfies about 3½% of that demand. Since we are a relatively small player in this market we need to be efficient to remain competitive. We cannot afford unnecessary cost burdens. Failure to resolve the concerns with the regulations that I have mentioned will result in further unnecessary cost burdens.

As I believe my testimony has made clear, we at CITGO believe promulgation of the current regulations implementing changes in the gasoline excise tax was a poorly thought through process. We would expect that the Internal Revenue Service had learned a lesson from that process; however, it appears that history is repeating itself in IRS implementation of similar changes in the law with respect to diesel and aviation fuel excise tax. In fact, if anything, the situation with respect to diesel and aviation fuel excise tax regulations is even worse. The statutory changes involving those taxes take effect April 1, 1988, and yet, to date no regulations have been issued and no public hearings scheduled. Again, the industry is faced with no clear, concise and consistent guidance for compliance with these latest statutory changes.

The diesel and aviation fuel sector of the industry is similar in most respects to the gasoline sector. Bulk transfers and exchanges among producers are critical. There are numerous large and small players, some of whom are exempt from the tax, some who are not. Participants range from major airline and manufacturing companies to small family farmers. Therefore many of the problems that plague the gasoline tax implementation process are relevant to implementation of the statutory changes for the diesel

and aviation fuel taxes. Some of the regulatory "fixes" that were finally achieved for gasoline tax collection are not going to be possible with respect to diesel and aviation fuel tax collection because of differences in the statutory scheme. The IRS has issued an Advance Notice of regulations to implement the diesel and aviation fuel tax. If regulations are promulgated along the lines suggested in that Advance Notice, serious problems will result in many areas, including the bond requirement; anti-competitive results of disparate treatment of participants; cash flow problems for exempt purchasers, such as farmers and state and local governments who must pay the tax and then seek refunds; and exchange transactions. The statutory changes for the diesel and aviation fuel tax were enacted in December, 1987. It is understandable that, with little more than three months between enactment and the effective date of the change, implementation by the IRS and compliance by the taxpayer would be wrought with confusion. The new law enacted major changes in the way these taxes are collected, and CITGO hopes that Congress will extend the effective date of these changes so that the major disruptions the industry has been going through with respect to the gasoline tax will not be repeated so needlessly with the diesel and aviation fuel excise tax.

I appreciate being able to provide these comments on behalf of CITGO. Both CITGO and I are willing to provide any further assistance on these issues that the Committee might find helpful.

STATEMENT OF SENATOR THAD COCHRAN

BEFORE THE

SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION

SENATE FINANCE COMMITTEE

HEARING ON COLLECTION OF FEDERAL FUEL TAXES

MARCH 16, 1988

Mr. Chairman, I commend you for holding this hearing to review the impact of recent changes in collection procedures on gasoline, diesel and special motor fuel taxes.

As we have all learned in recent weeks, these changes, if allowed to take effect on April 1 as scheduled, would have devastating effects on farmers and other tax-exempt users of diesel fuel.

Farmers, water carriers and others who purchase diesel fuel and gasoline for off-highway purposes have no federal tax liability for these purchases, but, under the new law, are required to pay these taxes initially and apply for a refund later.

The net result is no new tax revenue to the government, but merely an expensive double-handling of monies and paperwork.

Many of the industries which consume diesel fuel off our nation's highways are the very industries which have suffered severely over the past several years and are struggling to rebuild. For agricultural producers, the new requirement will significantly add to the upfront costs of production, while draining farmers of much needed operating funds. For river barge operators, upfront payment of tax not

owed will tie up funds necessary to pay boat crews and suppliers.

A water carrier in my State which employs fewer than 400 employees estimates that, under the new law, his firm would be loaning the federal government in excess of $500,000 per year, interest free, when no tax is owed.

Mr. Chairman, there is no reason why the government should have the use of these funds when there is no tax liability on these purchasers in the first place.

I hope that the Finance Committee will act promptly to approve legislation introduced by Senator Gramm and cosponsored by myself and other Senators to provide relief to agricultural producers and other off-highway consumers of diesel fuel. S. 2003 and S. 2118 would permit these users to continue the tax-free purchase of diesel fuel for off-highway purposes.

I support efforts to minimize the opportunity for avoidance of the diesel tax. However, I urge the subcommittee to examine alternative means for addressing this problem without imposing undue burdens on exempt users of this fuel.

Statement of
R. Timothy Columbus
on behalf of the
Society of Independent Gasoline Marketers of America

Regarding the Collection of Excise Taxes on Diesel Fuel

March 16, 1988

My name is R. Timothy Columbus. I am a member of the law firm of Collier, Shannon, Rill & Scott and appear today on behalf of our client, the Society of Independent Gasoline Marketers of America ("SIGMA").

SIGMA is a national trade association comprised of approximately 295 independent marketers and private brand chain retailers of motor fuels. SIGMA's members sell motor fuels in all 50 of the states and their sales represent between 15 and 20 percent of the retail market for motor gasoline.

SIGMA's members do not produce or refine crude oil. Thus, they are entirely dependent upon third parties for their supplies of motor fuels. As a result, they have built their business based upon their marketing efficiencies. Specifically, by innovating such cost-savings techniques as self-service and high volume/low margin marketing, SIGMA's members have reduced the amount of fixed operating costs which must be recovered in the per gallon selling price charged to consumers. These cost efficiencies have enabled them to compete effectively with their integrated supplier-competitors.

SIGMA respectfully suggests to the Subcommittee that it seriously consider repealing the provisions of the Revenue Act of 1987 (Pub. L. No. 100-203) ("the Act") which, effective April 1 of this year, will change the point of collection for the federal excise tax on diesel fuel. SIGMA believes that such action is necessary to: (1) alleviate the substantial hardships imposed upon the tax-exempt community which have given rise to this hearing, and (2) avoid a significant increase in evasion of the excise tax on diesel fuel to the detriment of the government's revenues and legitimate competitors in the diesel fuel market.

The underlying justification for the changes in the system for collecting the excise tax on diesel fuel was to enhance the Federal Government's revenues by reducing tax evasion and accelerating the collection of the tax, thereby enhancing the government's float on its revenues. Unfortunately, as other witnesses today will testify, the cost of accelerating the collection of the diesel fuel excise tax is likely to be borne primarily by entities for whom such costs represent a severe hardship. Moreover, it is SIGMA's heartfelt belief that the change in collection procedures provided for in the Act

will result in a significant increase in tax evasion rather than a reduction in that phenomenon.

SIGMA's conclusion that the new collection procedure for the excise tax on diesel fuel will result in a significant increase in tax evasion, and corresponding reduction in revenues, is based upon three factors: (1) the fact that all diesel fuel is home heating oil, (2) the amount of money which can be generated through tax evasion, and (3) the relative ease with which such transactions can be structured to frustrate traditional enforcement efforts. An understanding of these three factors will demonstrate why an increase in tax evasion is virtually unavoidable.

At the outset, members of the Subcommittee should recognize that all diesel fuel can be used as home heating oil. Specifically, the principal basis upon which the two fuels can be differentiated is the cetane rating of fuel qualifying as diesel fuel. In many areas of the country, pipeline specifications require that any no. 2 distillate fuel meet the cetane requirements for diesel fuel. Under such circumstances, the only real way to know whether no. 2 fuel is home heating oil or diesel fuel (and thereby properly subject to tax) is to know how it is in fact used. Normally, this determination can only be made upon the sale to the end user.

The prospective enforcement problem which the change in collection procedures will induce is enormous. Specifically, there will be two obvious means by which to evade the excise tax on diesel fuel. First, a wholesale distributor can simply purchase product as home heating oil and sell it as diesel fuel. An unscrupulous distributor clearly will not report this activity, but instead simply pocket the excise tax. Second, an unscrupulous marketer can purchase diesel fuel on an exempt basis and then resell that product through a number of shell corporations. At some point in its passage through this daisy chain, the product will be invoiced as "tax paid." Thereafter, it can be resold and the purchaser will be able to rely justifiably on its seller's representation. This second scenario is identical to the tax evasion daisy chains which were uncovered with respect to gasoline in the metropolitan New York area. It is mystifying as to why Congress, having changed the gasoline excise tax collection system to avoid this problem, has altered the diesel excise tax collection system to recreate it.

There is no question but that the excise tax on diesel fuel has been the subject of evasion in the past. Basically, there were two types of retailers: (1) law abiding, and (2) tax evading. The Act's changes in the diesel fuel excise tax collection system have created a situation in which law-abiding retailers will be offered "deep

discount" diesel fuel by disreputable marketers. Given the amount of money involved in the federal excise tax on diesel fuel, a disreputable marketer will be able to discount its product in sales to retailers substantially and still realize enormous profits. The sums which can be illicitly obtained by this method are of such a magnitude as to virtually guarantee that organized crime will involve itself in the process.

If SIGMA's fears are realized, then the anticipated revenue benefits of the change in the collection system will not be achieved. To the contrary, the Treasury will experience a loss of revenues. Moreover, the unlawful activity which will generate such losses will have a significant and detrimental effect on the competitive viability of legitimate marketers and retailers. Thus, the desired benefit will not be obtained and a clearly unintended injury to competition will be inflicted.

If Congress elects not to repeal the Act's changes in the collection procedure, it at a minimum should amend the Act's definition of the term "producer" to include chain retailers within that definition. The Act's definition of the term "producer" essentially is identical to the definition of that term previously used in the gasoline excise tax collection system in all respects save one -- it does not include chain retailers.

Chain retailers, i.e., firms which supply ten or more commonly-controlled outlets, perform all of the distributive functions performed by wholesale distributors. Specifically, they obtain the product and transport and deliver it to a retail distribution system. By excluding such firms from the definition of producer, the Act imposes on these firms costs not imposed upon other entities with which they compete. Given the small number of firms which correcting this situation would add to the roles of taxpayers, and the significant inequity which their exclusion creates, it is eminently reasonable to request that the Act's definition of "producer" be amended to include them.

SIGMA would also like to take this opportunity to share with the Subcommittee its concerns regarding the recently-implemented changes in the gasoline excise tax collection system. Specifically, SIGMA wishes to bring to the Subcommittee's attention two limited, but significant problems. First, Congress did not repeal section 6416 of the Internal Revenue Code as it applies to sales of gasoline to tax-exempt entities. The new system for collecting taxes on gasoline poses a significant threat to independent marketers' ability to compete for the business of tax-exempt entities, such state and municipal governments. This problem arises because the only entity entitled to take a tax credit against its liability on the gasoline excise tax for gallons sold to such tax-exempt organizations are those entities which will qualify as taxpayers. The amendments contained in the 1986 Tax Reform Act exclude from the class of entities

which may qualify as taxpayers those marketers who obtain their supplies exclusively at the terminal rack. Thus, such marketers can only sell to tax-exempt entities on a tax-free basis if their suppliers are willing to accept a certification from the marketer that particular volumes are designated for tax-exempt customers. Some suppliers of gasoline to independent marketers already have indicated that they will not accept such certifications. As a result, these marketers will effectively be foreclosed from serving state and municipal governments which, because of their own financial demands, will insist on buying gasoline only from entities which can sell to them on a tax-free basis.

The second problem relating to the new system for collection of gasoline excise tax which SIGMA believes must be addressed by Congress as soon as possible relates to the truck blending of gasoline and ethanol to make gasohol. Specifically, truck blenders of gasohol historically have been entitled to purchase gasoline at a reduced rate of excise tax which reflects the ultimately lower tax imposed on the finished product gasohol. Truck blenders' ability to purchase gasoline at this reduced rate serves as the primary inducement for them to manufacture and market gasohol. However, the new system for collecting gasoline excise taxes raises serious questions regarding the future viability of gasohol manufactured through truck blending.

Under the new gasoline excise tax collection system, marketers who purchase gasoline under the terminal rack and then blend it with ethanol obtained at a different location may be required to pay the full 9.1 cents per gallon excise tax on gasoline and seek a refund. The result of this process is to reduce significantly, if not eliminate, the primary inducement to manufacture and market gasohol which has been truck blended.

Last year, SIGMA's members marketed approximately four billion gallons of gasohol. The corresponding benefits of marketing gasohol have enabled SIGMA's members to remain aggressively competitive with respect to price. Should those benefits be eliminated, SIGMA's members will lose a significant competitive tool and ethanol producers will lose a significant market.

Both of the problems which SIGMA raises with respect to the gasoline excise tax collection system can be addressed and alleviated quite simply. Specifically, the enactment of legislation, similar to that propounded last year by Congressman Pickle in technical corrections legislation reported by the House Ways and Means Committee would enable marketers to compete for the business of state and local governments as well as continue to receive the benefits which Congress intended for truck blenders of

gasohol. Thus, SIGMA urges the Subcommittee to approve and report promptly legislation similar to that proposed by Congressman Pickle.

Finally, it is important that I communicate one general, but in SIGMA's view, enormously important observation. The changes in the systems for collecting the diesel and gasoline excise taxes which Congress has enacted were to a substantial extent premised on an accurate view that the Treasury was losing funds to tax evasion. However, these changes have not closed off the possibility, and perhaps more appropriately the probability, of continued evasion. Moreover, while failing to achieve one of their primary objectives, they have generated significant hardships to law abiding citizens. The saddest part of this reality is that Congress has available to it an alternative which would substantially reduce the possibility of tax evasion while creating minimum hardships for marketers and consumers of motor fuels. Specifically, Congress could provide the Internal Revenue Service funds for and direction to tie the motor fuels excise tax collection system into an electronic data processing system. Such an investment by Congress would be significant. However, it would quickly pay for itself.

Congress and the Internal Revenue Service could work with the petroleum industry to devise a reporting system which would, with a minimum burden to industry, maximize the Internal Revenue Service's ability to identify tax fraud promptly. Such a system would enable the limited staff available to the Service to promptly identify targets for enforcement action and terminate evasion schemes quickly. This type of enforcement is the only single thing that can provide sufficient deterrent to insure that evasion is minimized and that the Treasury collects the revenues which Congress intended.

SIGMA appreciates this opportunity to share its views with the Committee. I will be happy to respond to any questions which my testimony may have raised.

STATEMENT OF CONGRESSMAN HAL DAUB TO THE
SENATE FINANCE COMMITTEE
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
COLLECTION OF THE DIESEL FUEL EXCISE TAX
MARCH 16, 1988

MR. CHAIRMAN, THANK YOU, AND YOUR COMMITTEE MEMBERS, FOR ALLOWING ME TO SPEAK BEFORE YOU TODAY ON THIS IMPORTANT TOPIC. AS A MEMBER OF THE WAYS AND MEANS COMMITTEE FROM AN AGRICULTURAL STATE I SEEM TO HAVE BECOME SOMEWHAT OF AN EXPERT IN TAXATION OF FARMERS THAT USE DIESEL FUEL FOR EXEMPT PURPOSES. AS YOU ARE PROBABLY AWARE, FARMERS WILL FACE FUEL COST INCREASES OF APPROXIMATELY 15%, BEGINNING APRIL 1 OF THIS YEAR, APPROPRIATELY KNOWN AS APRIL FOOLS DAY.

TO BEGIN, I WOULD LIKE YOU TO KNOW THAT I HAVE HAD A SERIES OF MEETINGS WITH THE IRS COMMISSIONER, LARRY GIBBS, OVER THE PAST FEW WEEKS, AND I HAVE ASKED, TOGETHER WITH OTHER MEMBERS OF MY COMMITTEE, THAT HE AID US BY PROVIDING A TEMPORARY STAY TO THE IMPOSITION OF THIS TAX UNTIL CONGRESS HAS HAD AN OPPORTUNITY TO ADDRESS THE ISSUE. I REGRET TO INFORM YOU THAT ALTHOUGH MR. GIBBS WAS SYMPATHETIC TO THE PLIGHT OF THE FARMERS, HE FELT THAT HE COULD NOT TAKE THE LAW INTO HIS OWN HANDS, SO TO SPEAK, AND TOLD ME THAT THE CONGRESS WOULD HAVE TO ADDRESS THIS ISSUE WITH A LEGISLATIVE SOLUTION.

UNFORTUNATELY, I DO NOT EXPECT MY COMMITTEE TO BEGIN THE MARK-UP OF A TAX BILL UNTIL THE END OF THIS MONTH WHEN WE TAKE UP TECHNICAL CORRECTIONS AGAIN. THE FACT IS, THAT BARRING AN UNUSUAL LEGISLATIVE REMEDY, THIS LAW WILL NOT BE REPEALED UNTIL AFTER THE EFFECTIVE DATE, APRIL 1, PASSES. IT IS MY UNDERSTANDING THAT YOUR COMMITTEE INTENDS TO BEGIN THE MARK UP OF A BILL THAT WILL DEAL WITH THE COLLECTION OF THE DIESEL FUEL TAX WITHOUT IMPOSING HARDSHIPS ON EXEMPT USERS. I COMMEND YOU FOR EXPEDITING THIS BILL AND WANT YOU TO KNOW THAT I WILL DO EVERYTHING I CAN TO SEE THAT THE WAYS AND MEANS COMMITTEE ALSO ACT QUICKLY SO THAT WE WILL REPEAL THIS UNFAIR TAX PRIOR TO THE EFFECTIVE DATE OF APRIL FIRST.

I WOULD LIKE TO STRESS TO YOU THAT THE PLIGHT OF THE FARMER IS AN UNUSUALLY DIFFICULT ONE FOR THESE REASONS. FARMERS DO NOT FILE ESTIMATED TAXES. NEITHER DO THEY HAVE WITHHOLDING FROM WAGES AS DO MOST AMERICANS. INSTEAD, CONGRESS IMPOSED AN EARLIER FILING DATE FOR FARMERS TO FILE THEIR TAX RETURNS. THE DATE IS MARCH 1ST. IN SHORT, FARMERS HAVE AN EXAGGERATED CASH FLOW PROBLEM BECAUSE THEY MUST WAIT THE ENTIRE YEAR BEFORE THEY CAN RECEIVE THE MONEY DUE THEM . . . WHICH THEY NEVER DID OWE. TAXPAYERS WHO MAKE ESTIMATED TAX PAYMENTS HAVE AN OPPORTUNITY FOR SOME RELIEF BECAUSE THEY CAN REDUCE THE AMOUNT OF TAX PAID WITH THEIR QUARTERLY FILINGS. TAXPAYERS WHO HAVE WITHHOLDING CAN INCREASE THE NUMBER OF EXEMPTIONS CLAIMED ON THEIR W-4 FORM TO TAKE INTO ACCOUNT THE AMOUNT OF INCREASED TAXES PAID THROUGH THE DIESEL FUEL TAX. FARMERS HAVE NO SUCH OPPORTUNITIES.

MY POINT FROM ALL THIS IS THAT FARMERS ARE AN EXTREME CASE. SOON THEY WILL BEGIN PAYING A NEW TAX WHICH WILL ADD TO THEIR CASH FLOW PROBLEMS, THEIR INTEREST COSTS, AND THEIR ADMINISTRATIVE FILINGS WITH THE GOVERNMENT.

THIS IS A REVENUE ISSUE, BUT IT IS NOT A COMPLIANCE PROBLEM. FARMERS DO NOT USE DIESEL FUEL FOR ROAD USE AND SO THEY ARE NOT BEING PENALIZED FOR NONCOMPLIANCE. THIS IS A CASH FLOW ISSUE, AND THE GOVERNMENT WILL BE FUNDING ITSELF ON THE FLOAT OF THE AMERICAN FARMERS MONEY. THE ACCELERATION OF THE PAYMENT OF THIS TAX, FOLLOWED BY ITS REFUND, BECAUSE OF THE TIMING OF THE GOVERNMENT'S FISCAL YEAR, RESULTS IN ABOUT A $100-150 MILLION GAIN TO THE GOVERNMENT DURING FISCAL 1988. IN LATER YEARS THIS PROVISION WILL ACTUALLY LOOSE REVENUE, I AM TOLD. I FELT THAT THIS WAS RIDICULOUS TAX POLICY AND SO ON THE FIRST DAY OF THE NEW SESSION I INTRODUCED MY BILL, H.R. 3844.

IT CONTAINS THREE PROVISIONS THAT I BELIEVE YOUR SUBCOMMITTEE SHOULD ADDRESS DURING YOUR MARK UP ON FRIDAY. FIRST, IT REINSTATES THE EXEMPTION FROM THE DIESEL AND THE GASOLINE TAX FOR FARMERS. SECOND, IT CONTAINS THE SO-CALLED "PICKLE AMENDMENT" WHICH WOULD ALLOW REGISTERED WHOLESALE

DEALERS TO PURCHASE GASOLINE WITHOUT PAYING THE TAX TO THE REFINERY OR TERMINAL IF THEY ARE BONDED OR SUPPLY PROOF OF FINANCIAL RESPONSIBILITY. FINALLY, IT ADDRESSES THE PROBLEMS CAUSED BY CHANGES IN THE TAX REFORM ACT THAT REQUIRE THE PAYMENT FOLLOWED BY THE REFUND OF THE TAX ON GASOLINE USED TO BLEND GASOHOL. THE IRS HAD ISSUED REGULATIONS IN DECEMBER AS TO THE PAYMENT OF THE FULL TAX, FOLLOWED BY A REFUND OF MOST OF THE TAX 20 DAYS AFTER FILING FOR A REFUND. THESE REGULATIONS WOULD HAVE BEEN DEVASTATING TO THE ETHANOL INDUSTRY, BUT THEY WERE WITHDRAWN AND HAVE JUST BEEN DELAYED FOR A SECOND TIME UNTIL JULY. IT IS MY FEAR THAT IF CONGRESS DOES NOT SOLVE THE PROBLEM, UP TO 80% OF THE BLENDERS WILL QUIT BLENDING AND OUR FARMERS WILL LOOSE AN IMPORTANT MARKET FOR THEIR GRAIN.

I HOPE THAT YOU WILL BE ABLE TO ADDRESS THESE CONCERNS, AS WELL AS THOSE OF OTHER EXEMPT USERS OF DIESEL FUEL SUCH AS CONTRACTORS AND OIL DRILLERS, AND IF I CAN BE OF ANY HELP TO YOU I HOPE YOU WILL CONTACT ME.

Statement by
JAMES C. DAY
President and CEO
Noble Drilling Corporation
Tulsa, Oklahoma

Mr. Chairman and members of the Subcommittee, my name is Jim Day and I appear today on behalf of the International Association of Drilling Contractors (IADC), the Association of Oilwell Servicing Contractors (AOSC), and the International Association of Geophysical Contractors (IAGC).

I am President and C. of Noble Drilling Corporation headquartered in Tulsa, Oklahoma. My company is involved in both onshore and offshore drilling activity, and is among IADC's largest members. I also serve as IADC's Government Affairs Committee chairman. IADC is a trade association representing virtually the entire domestic oil and gas drilling industry, including over 1,200 companies. AOSC is the trade association for the well-service contracting industry, including over 650 member companies. IAGC, representing approximately 160 companies, is the trade association including geophysical (seismic) companies, and geophysical departments of integrated oil companies, which do virtually all of the petroleum geophysical exploration development work in the United States, and about 95% of such work outside the United States. As is evident from these descriptions, these trade groups represent a most significant and vital part of the domestic oil and gas industry, broadly defined, running the gamut from the business of exploring for sources of oil and gas to that of maintaining existing producing wells.

Each of these industry groups is terribly concerned about the imminent change in the collection of the 15.1 cent excise tax levy on diesel fuel, as sought by the Internal Revenue Service (IRS). This change in collection procedures was facilitated by enactment of the Omnibus Budget Reconciliation Act of 1987. I doubt very much it would have survived scrutiny as a free-standing item, and I've no doubt that's precisely why it was embedded in the omnibus bill. Nevertheless, drilling, well-

servicing, and geophysical contractors who consume large volumes of diesel fuel and who are at least theoretically exempt from the excise tax levy are faced with a devastating cash-flow impact if forced to pay the levy as will be required effective April 1. The IRS hasn't demonstrated abuses by our industries in the utilization of diesel fuel. In fact, very little justification for the change in collection procedures has been offered, except general statements that revenue-losing abuses have occurred.

Our companies, as is well known, are in a chronic state of depression which has lingered for some five years, and which shows no sign of abating. To be visited with a cash-flow raid of the magnitude presented by the IRS on April 1 will be a further significant attack on the already anemic financial state of our industry groups, and could be fatal for smaller companies.

For drilling contractors, that point is illustrated best in the light of fairly recent history. Keep in mind that drilling contractors--and well-servicing contractors and geophysical contractors--don't have an interest in the oil or gas produced. Thus, we're much more susceptible to business cycles which don't adversely affect our customers, the oil companies, many of which can continue to profitably produce oil, albeit at reduced profit margins, or who import foreign oil and make money in the refining and marketing of it. Five years ago, there were 5,500 drilling rigs available for work. Through deterioration and cannibalization, only 3,000 rigs are now deemed available for work, and of that number less than a third are working. An average land rig uses approximately ~~29,000~~ 290,000 gallons of diesel per year, and an offshore rig consumes over 612,000 gallons of diesel fuel in a year. Of IADC's member companies, perhaps two realized a profit in 1987.

For well-servicing contractors, only 54% of the existing 6,227 rigs are working. An average servicing rig consumes approximately 25,000 gallons of diesel annually. For the geophysical industry, but 175 crews are working in the onshore

United States: this is a small fraction of the activity just six years ago, when 741 crews were working. Extrapolating from the number of current seismic crews working in the U.S., the geophysical industry consumes upwards of 1,687,000 gallons of diesel a year. For marine seismic work there are 30 geophysical vessels operating in U.S. waters, with an annual consumption of 1.8 million gallons of diesel.

Essentially all contract drilling work is done at a stationary location. As might be expected, the drilling of a hole through rock and other strata is an energy-intensive process, requiring vast amounts of diesel fuel. Just so, 95% of well-servicing work is done "off road", and well-servicing rigs resemble drilling rigs in their operation. And, as far as seismic crews are concerned, approximately 95% of their activity is off road since most seismic work is conducted in the wild, so to speak, where no exploration has yet been, or is currently being conducted.

It's safe to say that this issue of the diesel fuel tax levy is the highest priority among the three trade groups I represent today. We find it absurd, at the least, that because of perceived abuses by other users of off road diesel that we should be caught up in their net, even while the IRS concedes that we remain "tax-exempt". We will shortly have to pay the tax, anyway, effectively giving the U.S. Treasury an interest free loan of precious capital, which we simply can't spare. We aren't operating from retained earnings, or accumulated profits. With a stripping away of cash-flow we simply will wither and die. Surely the Treasury, even if there are demonstrable abuses, could design a means of certifying that purchasers of diesel fuel are indeed applying their purchases to tax-exempt purposes. The Congress has heard a hue and cry from innocent bystanders like ourselves, and it's up to the Congress to repeal or greatly modify this ham-fisted approach to the IRS's administrative problems.

TESTIMONY OF SENATOR ALAN J. DIXON
BEFORE THE SUBCOMMITTEE ON
ENERGY & AGRICULTURAL TAXATION
THE MOTOR FUELS EXCISE TAX
MARCH 16, 1988

I WISH TO COMMEND SENATOR BOREN AND THE MEMBERS OF THIS SUBCOMMITTEE FOR THEIR WISDOM IN HOLDING A HEARING ON THIS ESSENTIAL TOPIC. AS MANY OF US ARE KEENLY AWARE, THE COLLECTION PROCEDURES FOR THE FEDERAL EXCISE TAX ON MOTOR FUELS HAVE RESULTED IN MANY SERIOUS PROBLEMS FOR A LARGE PORTION OF AMERICAN TAXPAYERS. THIS TAX TREATMENT, AS IT STANDS TODAY, HAS ADVERSELY AFFECTED FARMERS, STATE AND LOCAL GOVERNMENTS, EDUCATIONAL INSTITUTIONS, AND MANY SMALL BUSINESSES THROUGHOUT OUR COUNTRY.

MR. CHAIRMAN, CHANGES IN THE COLLECTION PROCEDURES ARE THE RESULT OF PROVISIONS IN BOTH THE TAX REFORM ACT OF 1986 AND THE RECONCILIATION ACT OF 1987. THE RATIONALE FOR CHANGE WAS THE GROWING CONCERN THAT THE FEDERAL GOVERNMENT WAS LOSING SUBSTANTIAL REVENUES DUE TO UNDERREPORTING, TAX EVASION, AND CHEATING. AS A RESULT, WE ATTEMPTED TO DEVISE A METHOD IN WHICH INCREASED COMPLIANCE COULD BE ENSURED, AND THE ABILITY OF THE IRS TO DETECT FRAUD ENHANCED.

NEITHER THE TAX REFORM ACT OF 1986 NOR THE RECONCILIATION ACT OF 1987 ALTERED THE TAX LIABILITY OF THESE GROUPS. THESE GROUPS WERE TAX-EXEMPT BEFORE THOSE ACTS WERE PASSED INTO LAW AND THEY REMAIN SO TODAY. WHAT HAS CHANGED, HOWEVER, IS THAT THESE GROUPS MUST NOW PAY THE TAX UP-FRONT, AND THEN APPLY AND WAIT FOR A REFUND FROM THE GOVERNMENT. TODAY, FARMERS, LOCAL GOVERNMENTS AND SMALL BUSINESSES ARE REQUIRED TO PROVIDE GOVERNMENT WITH AN INTEREST-FREE LOAN. IN ADDITION, WE HAVE FORCED UPON THESE GROUPS HIGHER OPERATING COSTS, AS WELL AS A DIMINISHING CASH FLOW.

MR. CHAIRMAN, THE HEARING YOU ARE HOLDING TODAY IS TESTIMONY TO THE FACT THAT MANY OF US IN CONGRESS HAVE COME TO VIEW THIS CURRENT POLICY AS INHERENTLY UNFAIR. ALTHOUGH IN THEORY IT HAD SOME MERIT, IN PRACTICE IT WILL HAVE A DEVASTATING IMPACT ON THOUSANDS OF INNOCENT CITIZENS. THERE IS NO DOUBT THAT TAX EVASION MUST BE STOPPED, AND WHEN CHEATING OCCURS IT MUST BE PENALIZED. HOWEVER, THERE HAS TO BE A MORE EQUITABLE SOLUTION TO COMBAT THESE PROBLEMS.

THERE HAVE BEEN A NUMBER OF BILLS RECENTLY INTRODUCED IN AN ATTEMPT TO FIND SUCH A SOLUTION. THESE BILLS, WHILE DIFFERING IN APPROACHES AND THEMES, ARE ALL GOOD. NONE OF THEM, HOWEVER, ADEQUATELY ADDRESS THE ENTIRE ARRAY OF CONFLICTING REQUIREMENTS POSED BY THE CURRENT LAW.

MR. CHAIRMAN, THE PROBLEMS WE CONFRONT TODAY ARE, TO A LARGE EXTENT, THE RESULT OF PIECEMEAL AND PATCHWORK MEASURES FROM THE PAST. MANY OF US BELIEVE THAT TO CONTINUE SUCH AN APPROACH TO THIS PROBLEM IS NOT AN ADEQUATE RESPONSE. WHAT IS NEEDED IS A COMPREHENSIVE BILL TO CLARIFY THE MANY PRESSING ISSUES PERTAINING TO DIESEL, GASOHOL AND GASOLINE. TO THAT END, SENATOR NICKLES AND I HAVE TAKEN WHAT WE BELIEVE ARE THE BEST COMPONENTS OF PREVIOUSLY INTRODUCED LEGISLATION AND ADDED THEM TO SEVERAL NEW SECTIONS.

IT IS OUR BELIEF THAT THIS COMPREHENSIVE BILL, WHICH WE ARE INTRODUCING TODAY, WILL PROVIDE THE ESSENTIAL RELIEF TO WHICH THOUSANDS OF OUR TAXPAYERS ARE TRUELY ENTITLED.

THE MOTOR FUELS EXCISE TAX RELIEF ACT SEEKS TO ENSURE EQUITY AND BALANCE IN OUR TAX CODE. THE BILL DOES NOT EXPAND THE CLASSES OF EXEMPT TAXPAYERS. RATHER, IT SEEKS ONLY TO RESTORE TO THE HISTORIC CLASSES OF EXEMPT TAXPAYERS THE TRUE MEANING AND RIGHT OF THEIR EXEMPTION -- TAX EXEMPT PURCHASES. IT ALSO SEEKS TO CORRECT THE COMPETITIVE IMBALANCES IN THE MARKETPLACE WHICH HAVE RESULTED FROM THE CHANGES IN THE MOTOR FUELS COLLECTION PROCEDURES. FURTHERMORE, THIS BILL WILL ALLEVIATE THE UNFAIR AND BURDENSOME REQUIREMENTS NOW IMPOSED ON FARMERS, EDUCATIONAL INSTITUTIONS, STATE AND LOCAL GOVERNMENTS, AND SMALL BUSINESSES. IN SO DOING, THIS BILL WILL ALSO ALLEVIATE THE TREMENDOUS ADMINISTRATIVE COSTS OF SORTING AND PROCESSING HUNDREDS OF THOUSANDS OF REFUNDS WHICH THE IRS WILL INCUR IN THE PROCESS.

MR. CHAIRMAN, THIS HEARING TODAY VIVIDLY DEMONSTRATES THE NEED FOR CONGRESS TO ACT WITH QUICK RESOLVE IN THIS MATTER. IT IS ESSENTIAL THAT WE ADDRESS THE MANY PRESSING PROBLEMS POSED BY THESE CHANGES IN A COMPREHENSIVE AND BIPARTISAN APPROACH. WE URGE THIS SUBCOMMITTEE TO CAREFULLY REVIEW THE LEGISLATION SENATOR NICKLES AND I HAVE INTRODUCED.

STATEMENT OF SENATOR PETE V. DOMENICI ON

EXCISE TAXES FOR DIESEL FUEL THAT IS USED FOR FARMING PURPOSES

Mr. Chairman, let me begin by thanking you for holding this timely hearing, and for allowing me to present my views to the subcommittee. I shall keep my remarks brief.

I strongly favor legislation that would reinstate tax-free treatment for diesel fuel that is used for off-road farming and ranching purposes.

Currently there are several Senate bills which would correct the problems created by a recent change in our tax laws. And at this point, I don't believe it is necessarily important which bill moves forward. It is very important however, that Congress move a bill soon, because this will have a serious impact on farmers and ranchers in just two weeks -- beginning April 1, 1988. Not a very funny april fools' joke in this Senator's opinion.

Under the "old" system, farmers were exempt from paying the 15-cent-per-gallon excise tax on diesel that was used for farming or ranching purposes. They were simply exempt from this tax. They did not owe the tax.

Under the "new" system, farmers are still entitled to tax-free treatment for off-highway use. But under the recent change, farmers will be forced to pay the tax at the time of purchase. Farmers and ranchers can then apply for a refund at year-end, when they file their Federal taxes.

The Federal Government will, in essence, have free use of farmers' hard-earned money for as much as a year, even though these farm families don't owe the tax in the first place.

For some reason, farm use was not provided an up-front exemption. But diesel fuel that is used to plow a field or run an irrigation pump is a non-taxable use, and it should be exempt from start to finish. Therefore, I support legislation that corrects this situation by removing the requirement that farmers pay the tax at the time of purchase, returning the law to what it was prior to 1987.

The recently enacted tax change for diesel fuel was undoubtedly aimed at reducing fraud and abuse. But I don't believe the change did anything to strengthen enforcement of the tax law. Rather, it will simply require a lot more record-keeping for farm families.

In my mind, this whole issue is very similar to the record keeping requirements imposed by the Internal Revenue Service (IRS) a few years ago where owners of private vehicles used for business were forced to keep log books. Those who abused the system before will continue to do so. All the change did was to make life tougher for farmers by piling on more bureaucratic record-keeping rules.

As far as most farmers and ranchers are concerned, this is just another government-created hassle, just another instance where they are forced to keep records so the Government won't be inconvenienced while using their money.

Mr. Chairman, I for one cannot accept the recent tax change for diesel fuel. Therefore, I hope the Senate will act promptly on this legislation, since the new tax requirement becomes effective on April 1.

Farmers and ranchers in New Mexico and elsewhere should never have to feel the effects of this ill-conceived change in the tax laws. I urge all my colleagues to join me in supporting legislation to fix this problem.

PREPARED STATEMENT OF ELLIS D. EDWARDS

I am Ellis D. Edwards, Treasurer of the State of Oklahoma. I appreciate the opportunity to testify before the Subcommittee about the fuel excise taxes and their effect on state and local governments. I am here today representing the nation's governors, state legislators, state treasurers, mayors, and other state and local finance officials. First I am going to address the excise tax on gasoline, then I will address the excise tax on diesel fuel.

A Hidden Tax

Before the Tax Reform Act of 1986, states and localities were exempt from paying the federal excise tax on gasoline just as federal vehicles were exempt from state and local fuels and vehicle taxes. The Tax Reform Act did retain the exemption for states and localities, but it prohibited tax-free sales. Thus, states and localities, even though exempt, must pay the tax, and then seek a refund from the federal government. Meanwhile, the federal government continues to be exempt from the state and local taxes.

Clearly, the most seriously affected governmental units are police, fire, and other public safety departments. This is especially true since many of them were in the middle of their budget year when the refund provision became effective.

In actuality this so called exemption creates a hidden tax - states and localities lose money on the bookkeeping and administrative costs they incur while tracking the amount of tax paid, and they lose the use of the tax money while the federal government holds it.

Moreover, while states and localities are losing the use of this money, others are using it interest-free. The refiners and terminal operators have the use of the money until they remit it to the federal government.

Furthermore, the law does not set a time period within which the federal government must make the refund, thus creating cash flow problems for states and localities. Cash flow problems will also result from the rules governing when a government can apply for a refund. Only if $1000 or more is paid in tax during a quarter can a refund be filed immediately after the close of the quarter. Otherwise the refund must be requested annually. This delay puts smaller towns at a disadvantage and causes them to lose the use of those dollars - sometimes for a year or more.

A sampling of state and local entities illustrates the severity of this loss of cash flow:

- In Oklahoma, Oklahoma City, with a population of 445,799, uses 1,592,000 gallons of gasoline and will pay approximately $145,000 in tax. Tulsa has 360,919 residents, uses 1,742,072 gallons, and will pay $158,528 in tax. McAlester, with 18,418 residents uses 100,000 gallons and pays $9,100 while Grove, with 4055 residents, uses 16,000 gallons and pays approximately $1450 in tax.
- The state vehicles for the State of Wyoming use 3.5 million gallons of gasoline, costing the state $318,500 in tax.
- South Dakota's state fleet uses 600,000 gallons of gasoline and pays tax of $54,600. This does not include the highway patrol.
- In Hawaii, the City of Honolulu uses 2,525,000 gallons of gasoline, which costs the city $229,775 in taxes.
- The Colorado Department of Education, with 176 school districts and 4700 school buses that travel 55.5 million miles to cover those districts, will use an estimated 12 million gallons of gasoline a year. The $1.1 million tax paid is considered a liability on the Department's books and so it cannot be used for educating students until it is returned by the federal government.

It's Going to Cost the Federal Government Too

One of the drawbacks of not giving this provision more consideration is that there are approximately 83,000 state and local governments and special districts that are eligible to apply for refunds. With a number of governments eligible to make quarterly filings because they pay $1000 or more of tax in a quarter, there could be upwards of 200,000 annual filings for refunds. The federal government will have to pay for this refund process.

Administrative Costs

Earlier I mentioned there were administrative costs for states and localities paying the tax and seeking the refund. It is important that you know what that entails.

First, someone has to keep track of how much tax has been paid. This presents a problem for small towns which have few or no full-time staff to file the refund or to follow-up to assure that the refund is received. Larger counties and cities that have staffs will have to increase their number of employees to accommodate the refund procedure. Someone has to keep track of the gasoline that all those departments purchase. The department of public works buys gasoline, the fire department buys gasoline, the police buy gasoline. Even libraries buy gasoline so they can have their bookmobiles go to people who might not otherwise be able to get books.

It would be easier if each department were able to apply for its own refund, but the IRS has told us that every department or section of government that uses the same Employer Identification Number (EIN) for taxpayer purposes must file for a refund on the same form. This creates a major problem. For example:

- In Maryland, all state departments, from the Department of Natural Resources to the University system use the same EIN, thus the state may use only one form to file for the refund for the tax paid by the entire state.

Maryland is not alone with its problems:

- o California is investigating three options to deal with the tax:
  1. Establish a separate office to centralize the refund procedure for the state's 300 agencies and departments.
  2. Have the departments that are major users of gasoline obtain their own Employer Identification Numbers.
  3. Renegoiate the the contracts the state already has with 41 gasoline vendors to have them sell the gasoline tax-free to the state. This would put the financial burden on the vendors, a number of whom are minority-owned firms.

Each of these options would cost the state time and money.

- o In South Carolina, a change in state law is necessary in order for a state agency to receive its share of the gas tax refund when the refund is received in a different state fiscal year than the year the expenditure was made.

<u>If Evasion Is The Problem Enforcement Should Be The Solution</u>

I understand the motive for changing the point of collection of the tax was to avoid evasion. We support these efforts. Preventing tax evasion helps law-abiding taxpayers, as well as those of us who share in the benefit from the tax. However, we were exempt so had no reason to evade paying the tax, and neither the Treasury or the Congressional Research Service reports suggest that states and localities were responsible for the evasion problem. Stronger enforcement of the existing laws would have made more sense than putting the collection burden where it does not belong.

Section 6416, Limited Relief

An existing portion of the Internal Revenue Code, Section 6416, provides limited relief to states and localities, but it is clear that it does not help everybody. Because wholesalers and refiners voluntarily use this provision, state and local governments are at their mercy. Moreover, small governments that are more likely to purchase gasoline at the retail level are not helped by this section unless they purchase gasoline using a major oil company credit card and then only if the company has opted to use Section 6416.

Section 6416 allows wholesalers to sell tax-free to states and localities. But the wholesaler must have the agreement of the ultimate taxpayer - the refiner or terminal operator. While some refiners are honoring wholesalers' requests to sell tax-free, others are not. This puts governments in the position of having to pay the tax, or shop around for a supplier who is able sell tax-free. Moreover, there is concern that gasoline prices will rise because wholesalers that waive the tax will want compensation for their paying the tax and waiting for a refund.

One way to alleviate the problem is to adopt the "Pickle Amendment" contained in the House technical corrections bill, which would allow the wholesaler to offer tax-free sales to qualified purchasers without the permission of the refiner. The retention and stengthening of Section 6416 would allow wholesalers to act independently and stimulate competition.

As important as Section 6416 is to many state and local governments it is still not a complete solution. Some governments and wholesalers don't know about it. Many are not in an area of the country where there is enough competition between wholesalers to make 6416 a factor. Others are too small to have the clout to receive the benefits of 6416. These small governments can ill afford to pay the tax and wait an unknown period of time for the refund.

Solutions

Restore True Exemption

Changing this tax paying and refund procedure to the more sensible exemption that was previously in place is simple enough that it could be part of the technical corrections to the Tax Reform Act of 1986. Or it could be done through separate legislation that Senator Nickles has proposed in S. 2062 and Congressman Neal has proposed in H.R. 3892.

In addition, Senator Daschle has introduced S 2075 that would provide an administrative mechanism that would allow state and local governments to purchase diesel fuel tax-free. We support Senator Daschle, as well as the Chairman of this Subcommittee, Senator Boren, and the members of the Finance Committee who are co-sponsors in this effort. This approach is a good beginning but incomplete. As the Committee moves to mark-up, we recommend that you address a comprehensive approach to the diesel and gasoline fuel excise tax burdens on states and localities.

Diesel Option

An alternative solution for gasoline would be to set up a system similar to the one that Secretary Baker has proposed in Internal Revenue Notice 88-30 concerning diesel where, upon receipt of certification from a state or local government, the wholesaler or refiner would sell tax-free and be able to receive a credit or refund. We commend the Secretary and the IRS for proposing a system that will greatly ease the burden on states and localities. The Notice says that states and localities will not be required to register or to pay the tax on diesel fuel they buy which has not already had the tax imposed. This is likely if they purchase from a registered wholesaler. If they purchase after the tax has been imposed, and themselves pay the tax, they can apply for a refund.

It appears that this system will be workable. However, as with Section 6416 with gasoline sales, it will not benefit the smaller governments - those who do not purchase enough diesel to merit having their own storage tanks and must buy retail, pay the tax and apply for a refund.

Conclusion

The refund procedure is a costly and unnecessary burden on taxpayers, states and localities, and the federal government. State and local governments have not abused the exemption, and should not have to bear the cost of combatting the evasion. Therefore a return to a true exemption is warranted.

The groups listed below have formed a coalition and are willing to work with Congress and the Department of Treasury to meet your needs to prevent evasion while maintaining the true exemption that states and localities should have.

Colorado Department of Education
Government Finance Officers Association
National Association of Counties
National Association of Fleet Administrators
National Association of State Budget Officers
National Association of State Treasurers
National Association of Towns and Townships
National Conference of State Legislators
National Governors' Association
National League of Cities
National School Boards Association
United States Conference of Mayors

STATEMENT OF SENATOR J. JAMES EXON (D-NE)
BEFORE THE
SENATE FINANCE COMMITTEE
ENERGY & AGRICULTURAL TAXATION SUBCOMMITTEE
MARCH 16, 1988
HEARING ON COLLECTION OF DIESEL FUEL
& GASOLINE TAXES

MR. CHAIRMAN, THANK YOU FOR ALLOWING ME TO GIVE YOU MY VIEWS AT THIS HEARING ON ISSUES INVOLVING COLLECTION OF FEDERAL TAXES ON DIESEL FUEL, GASOLINE, AND SPECIAL MOTOR FUELS.

FIRST, LET ME SAY THAT THE FINANCE COMMITTEE HAS ONE OF THE MOST DIFFICULT JOBS OF ALL THE SENATE COMMITTEES. TAXES WILL NEVER BE A POPULAR ISSUE AND TODAY IS NO EXCEPTION TO THE RULE.

MR. CHAIRMAN, AS A COSPONSOR OF S. 2075 INTRODUCED BY SENATOR DASCHLE, I SIMPLY WOULD LIKE TO ADD MY VOICE TO THOSE HERE TODAY WHO ARE, IN EFFECT, CALLING FOR A RETURN TO A MORE SIMPLE AND FAIR METHOD OF HANDLING OUR FEDERAL FUEL TAXES. THERE ARE A NUMBER OF ISSUES, BUT IN PARTICULAR, THE SCHEDULED APRIL 1 CHANGE IN DIESEL FUEL TAX COLLECTIONS I BELIEVE AFFECTS THE MOST PEOPLE. IF THE 1987 CHANGE IS ALLOWED TO GO INTO EFFECT, FARMERS WILL BE REQUIRED TO PAY A TAX THEY DO NOT OWE AND BE RESPONSIBLE FOR ADDED PAPERWORK TO GET A REFUND.

IT'S ONE THING TO TRY TO INCREASE OUR EFFORTS TO COLLECT TAXES THAT ARE OWED. BUT ITS QUITE ANOTHER THING TO INCREASE OUR EFFORTS TO COLLECT TAXES THAT ARE NOT OWED.

SOMEWHERE ALONG THE ROAD TO ALL THE RECENT "TAX REFORM" WE HAVE HAD THE LAST FEW YEARS, THE CONCEPT OF SIMPLICITY GOT LOST. THIS ISSUE INVOLVING FARMERS AND DIESEL TAXES IS, UNFORTUNATELY, ONLY ONE EXAMPLE.

I UNDERSTAND THE MOTIVES FOR THIS 1987 CHANGE, IN THAT THERE WAS A DESIRE TO REDUCE THE DEGREE OF "LEAKAGE" IN DIESEL FUEL TAX

COLLECTIONS. HOWEVER, WE SHOULD NOT MAKE THE "CURE WORSE THAN THE DISEASE" IN THE PROCESS OF TRYING TO ADDRESS THE PROBLEMS.

THE CHANGE IS ESTIMATED, ACCORDING TO THE AMERICAN FARM BUREAU, TO REQUIRE FARMERS TO PAY $420 MILLION PER YEAR IN DIESEL TAXES. THEY WOULD THEN HAVE TO WAIT FOR REFUNDS. MR. CHAIRMAN, YOU HAVE BEEN A LEADER AND HAVE JOINED ME IN PROVIDING FOR MORE OPERATING CAPITAL FOR THE NATION'S FARMERS. I BELIEVE YOU WILL AGREE WITH ME THAT NOW IS NOT A GOOD TIME TO REVERSE COURSE AND BORROW NEARLY HALF A BILLION DOLLARS IN OPERATING CAPITAL FROM OUR NATION'S FARMERS FOR UNCLE SAM.

MR. CHAIRMAN, THANK YOU AGAIN FOR CONSIDERING MY VIEWS TODAY AND FOR HOLDING THIS HEARING.

--end--

STATEMENT OF ROBERT E. FARRIS
DEPUTY FEDERAL HIGHWAY ADMINISTRATOR

FEDERAL HIGHWAY ADMINISTRATION
U.S. DEPARTMENT OF TRANSPORTATION

"COLLECTION OF GASOLINE AND DIESEL FUEL TAXES"

Good morning. I am Robert E. Farris, Deputy Administrator, Federal Highway Administration. With me today is Anthony J. McMahon, Chief Counsel for the Federal Highway Administration. I am pleased to be here to discuss the recent revisions in the collection procedures for gasoline and diesel fuel excise taxes.

Changes in the Collection Point of Diesel and Gasoline Taxes to Reduce Tax Evasion.

The short answer to the effectiveness of the recent changes is that it is too early to tell. Still, we do know that considerable Highway Trust Fund revenue is lost each year to fuel tax evasion. In 1987, actual trust fund receipts totalled $13.03 billion of which $11.6 billion (89 percent) was generated by motor fuel taxes. While it is difficult at this point to estimate the full extent of evasion, the President's budget estimates that an additional $688 million in receipts will be gained in 1988 through efforts to improve compliance.

Diesel fuel tax evasion activity poses a serious threat to an important source of highway revenue. Diesel fuel tax receipts amounted to approximately $2.8 billion in 1987. The Administration proposed last year a legislative initiative to reduce diesel fuel tax evasion, specifically, by raising the point of tax collection from the retail to the wholesale level. This proposal was adopted in the Omnibus Budget Reconciliation Act of 1987. The change, when implemented on April 1, 1988, will effectively reduce the number of fuel taxpayers from over 60,000 to about 8,000 nationwide, giving the Internal Revenue Service (IRS) a much better chance of enforcing compliance.

During 1985 and 1986, a combined diesel fuel tax enforcement test program was conducted under a Federal and State agreement. The objective of the project was to test the effectiveness of joint Federal/State audits. The results were extraordinary. Audits of 25 taxpayers in 5 States disclosed underpayment of Federal diesel fuel taxes of close to $2 million, equivalent to $80,000 per taxpayer.

Estimates of revenue increases from reduced diversion of diesel fuel taxes are sizeable. One State recently raised its point of diesel fuel tax collection and realized a 15-percent increase in revenues as a result of reduced tax evasion. The Department of Treasury estimates that improved compliance will produce an increase in highway tax receipts of $250 million per year and that when reduced income tax receipts are taken into account the net increase in Treasury receipts will be $200 million per year.

Gasoline tax revenues to the Highway Trust Fund totalled $8.8 billion in 1987. There is evidence that tax evasion has been a significant drain to this source of highway revenue. During testimony in 1986 relating to organized crime's diversion of Federal gasoline tax funds, one witness set his "take" at $8 million per week. All told, testimony was given asserting that up to $1 billion was being lost annually. If the $1 billion figure were valid, almost 10 percent of that year's tax receipts was lost to evasion. The multiplicity of taxpayers at the wholesale level was a leading cause of IRS's inability to assure compliance. Raising the point of gasoline tax imposition from the wholesale level to the terminal level, enacted in the Tax Reform Act of 1986 (TRA), reduced the number of taxpayers that IRS must monitor from about 8,000 to about 1,000, and gave the IRS a fighting chance at accurately auditing taxpayers.

The Federal-aid highway program is dependent on the user fee financed highway trust fund for funding. Accordingly, depletion of motor fuel tax by evasion activities poses a serious danger to

our Nation's highway programs in an era when highway travel has reached unprecedented levels.

Alternative Means of Collecting Diesel and Gasoline Taxes.

Because provisions of the Omnibus Budget Reconciliation Act of 1987 and Tax Reform Act (TRA) of 1986 moved the collection points for motor fuel taxes, certain tax-exempt users must now first pay diesel and gasoline taxes and subsequently file for a refund. This prepayment and refund process has generated widespread interest, and has led to many complaints by those who were not previously liable for payment of the tax.

On January 5, 1988, the IRS held a hearing to ascertain the concerns of those affected by the proposed gasoline tax regulations published in the Federal Register on November 18, 1987 to implement the gasoline tax collection provisions of the Omnibus Budget Reconciliation Act of 1987 and the TRA. FHWA has reviewed the public comments filed in the IRS docket and testimony during the IRS hearing and we believe that selected alternatives and variations for collecting gas and diesel fuel taxes offered by these groups warrant consideration. These proposals include permitting more frequent filing for refunds, say every 2 months, and would require the IRS to pay interest on refunds not remunerated after 30 days; allowing refunds to be based on the amount of fuel purchased, not merely the quantities used; and making use of Section 6416 of the IRS Code. However, we recognize the workload problems this may present to the IRS. In January, the IRS issued Notice 88-13, which is essentially a reminder that Section 6416 of the IRS Code is still in effect and should be used. While State and local officials were generally unaware of its existence at the time of the January 5 hearing, Section 6416 allows taxpayers that have paid the tax to sell gasoline at a tax-exempt price, to State and local governments, and apply to the IRS for a credit or refund.

FHWA does not support the continuance, contained in S. 2067,

after the April 1 deadline of the transitional rule contained in Notice 88-2, which allows gasohol blenders to purchase gasoline with the 6-cent exemption included in the price. According to IRS sources, it is uncertain whether these types of purchases will be permitted after April 1. In our view the opportunity for evasion under such a system is substantial.

As with the gasoline law changes, there have been numerous concerns expressed by those affected by the recent diesel fuel tax legislation, particularly States and local municipalities and agricultural interests. In weighing the costs and benefits of allowing States and local municipalities to purchase diesel fuel tax-free, FHWA believes it would be sound public policy to allow such purchases. On March 3, 1988, the IRS issued Notice 88-30 which generally indicates that the Secretary of the Treasury has decided to exercise his authority to permit tax-free purchases of diesel fuel for uses such as: diesel fuel for use in diesel-powered trains; aviation fuel for use in commercial aircraft; taxable fuel for use other than as motor fuel; and taxable fuel sold to a State or local government for its exclusive use. While all others must register for tax-free purchases, State and local governments will simply complete, and keep on file, a "Certificate of Registry." With this certificate on file, States and local municipalities will be able to make tax-free purchases for up to 12 calendar quarters (3 years) -- after which, the certificate will expire and necessitate recertification. Certain record keeping requirements would be imposed on both the seller and purchaser of such tax-free fuel sales.

Agricultural groups have expressed complaints of cash flow problems under the new diesel fuel tax laws, which are similar to those of State and local jurisdictions. A certification process for farmers similar to that provided for State and local jurisdictions could be considered. Any such process must satisfactorily resolve the difficult problem of who, at any given time, is a farmer. If IRS compliance efforts are not increased, a

certification process would continue opportunities for diesel tax evasion. In recognition of the problem posed by fuel tax evasion, FHWA's Fiscal Year 1989 budget proposal includes a request for $5.0 million to be reimbursed, under an interagency agreement, to the IRS to increase efforts to improve taxpayer compliance with highway excise taxes. Measures to be taken by the IRS would include improved taxpayer audit coverage, additional efforts to identify tax evaders, and improved coordination between IRS and State fuel tax audit activities. FHWA would prefer to see the results of the new legislation and increased enforcement efforts before further revisions are made.

That concludes my statement. I would be pleased to answer questions that you or members of the Committee may have.

Jerdy Gary, on behalf of the
Petroleum Marketers Association of America

Good morning Mr. Chairman and members of the Subcommittee. I am Jerdy Gary, Chairman of the Board of Sooner Oil Company in Denison, Texas. Sooner Oil has been in operation for over 30 years, supplying motor fuels through 35 retail outlets in Northern Texas and Oklahoma. I am also a Past President of the Texas Oil Marketers Association and a former member of the Board of Directors of the Petroleum Marketers Association of America (PMAA). I am here today representing PMAA.

PMAA commends the subcommittee for its active interest in the federal motor fuel excise tax collection issues in terms of both diesel fuel and gasoline. This hearing takes on ever more significance Mr. Chairman, in view of the announcement late last Friday afternoon that the full Finance Committee intends to mark-up legislation covering these issues on Friday, March 18.

The Petroleum Marketers Association of America is a federation of 43 state and regional associations which represent over 10,000 companies throughout the United States. Our 43 member associations are listed on Attachment I. Collectively, PMAA members account for approximately 50 percent of the gasoline, 60 percent of the diesel fuel, and 75 percent of the home heating oil sold in the United States. The majority of marketers sell their products in rural America; however, many marketers also operate in urban and suburban markets. Nearly 90 percent are classified as small business by SBA size standards. PMAA's average member company has 22 employees. A simplified flow chart of the petroleum distribution industry in the U.S. is shown as Attachment II.

Background

Mr. Chairman, PMAA has been working on the federal motor fuel excise tax issue for several years. Our efforts have been directed at both the collection of the 9.1 cents per gallon federal excise tax on gasoline and the 15.1 cents per gallon federal excise tax on diesel fuel. Congress dramatically changed the gasoline excise tax collection process effective January 1, 1988, as part of the Tax Reform Act of 1986 (PL 99-514). The diesel fuel change was enacted on December 22,

1987, as part of the Omnibus Budget Reconciliation Act of 1987 (PL 100-203).

These changes, along with the delays by IRS in the issuance of timely regulations to implement these changes, has led to tremendous confusion throughout the petroleum marketing industry. This confusion has spilled over to many of our customers including farmers, state and local governments, drilling contractors, marinas and many others.

Gasoline Excise Tax Collection Process: Congressional Action

Mr. Chairman, in Section 1703 of the Tax Reform Act of 1986 (PL 99-514), Congress changed the collection procedure for the 9.1 cents per gallon federal excise tax on gasoline. Under this procedure, which took effect January 1, 1988, the point of taxation is when gasoline leaves the terminal and is loaded into trucks for further distribution. The seller of the gasoline at that point, usually a terminal operator, refiner or importer, would collect the tax from the purchaser, usually a jobber or chain retailer, and remit it to the Internal Revenue Service on a specified payment schedule. Once the gasoline passes the point of taxation (i.e. loaded from the terminal into trucks) no further tax exempt sales are allowed. Purchasers of gasoline that previously bought on a tax exempt basis would have to pay the tax and apply for a refund.

Prior to enactment of Section 1703, the excise tax collection procedure was based on the first sale of gasoline from a "producer" to a non-producer of gasoline. "Producer" was defined to include not only refiners, terminal operators and importers, but also wholesale distributors and chain retailers. This meant that the taxable event could occur at several points in the gasoline distribution process. For example, the taxable event may not occur until the refiner or independent marketer sold product to a motorist at a station he owned and operated.

Gasoline Excise Tax Collection Process: Problems Resulting from Recent Change:

There are at least three problems with the new system which need to be addressed by technical corrections to Section 1703. First, the clear intent of Section 1703 is that there be no tax exempt sales downstream and that current tax exempt purchasers apply for a credit or refund of taxes paid. However, Congress inadvertently failed to repeal

Section 48.6416 of the Internal Revenue Code, which allows suppliers not to pass on to their state and local government customers the taxes already paid on gasoline, and file for a refund of the tax from the IRS. Unfortunately, under Section 6416, only "taxpayers" are eligible to apply directly to the IRS for the refund. Wholesale distributors/jobbers are no longer considered "taxpayers" and must apply to their refiner-suppliers for a refund of the taxes paid but not collected from the government entity.

The use of Section 48.6416 is voluntary on the part of the refiners, however, and some have indicated a willingness to honor this procedure, but several others have not. This means that many state and local governments served by wholesale distributors probably will be unable to take advantage of the provisions of Section 6416. Moreover, refiners have a built-in competitive advantage over wholesale distributors under Section 48.6416, in that they can sell to state and local governments tax free and deduct that amount from the taxes remitted directly to IRS. Jobbers on the other hand, must either wait for a refund from their refiners who have chosen to honor Section 48.6416, or must charge their exempt customers the tax. Even when the supplier agrees to a refund it may take an extended period of time for a marketer to receive his money.

The second problem relates to gasohol. Under Section 1703, purchasers of gasoline and ethanol blended at the same terminal are entitled to the reduced tax rate applicable to gasohol of 3 and 4/9 cents per gallon. However, purchasers who buy gasoline at one terminal and ethanol at another (few terminals sell both gasoline and ethanol) may have to pay the full 9.1 cents per gallon tax and apply for a refund from IRS. Currently, IRS is allowing purchasers of gasoline and ethanol from separate terminals the reduced tax rates. This transition rule has been extended to June 30, 1988. However, there are indications from IRS that effective July 1, only those gallons purchased and blended at the same terminal will be eligible for the reduced rate.

The final problem relates to the fact that in the petroleum industry, refiners are both suppliers and competitors of wholesale distributors/jobbers. By allowing the refiner to collect the tax from the jobber means the refiner has the use of the jobber's tax money for

as much as two to three weeks before the taxes must be paid to the government. The "float" on these tax dollars clearly give refiners a competitive advantage over jobbers.

Gasoline Excise Tax Collection Process: PMAA Solution

PMAA recommends that Congress enact one minor change to Section 1703 of the 1986 Tax Reform Act (PL 99-514). This change would allow purchasers of gasoline at the terminal to remit the federal excise tax directly to IRS, provided that the purchaser (wholesale distributor or chain retailer) is registered as a tax remitter and agrees to comply with any bonding or financial responsibility requirements imposed by the IRS. The point of taxation would remain the same (i.e. as product is loaded into trucks for the first time at the terminal). In addition, there would be no tax exempt sales of gasoline, except those authorized under Section 48.6416 of the Internal Revenue Code to state and local governments.

There are several advantages to this amendment. First, it would correct the competitive advantage refiners have over marketers by giving marketers the right to remit the tax directly to IRS based on their purchases from the refiner. Secondly, it would allow those state and local governments supplied by wholesale distributors/jobbers to take advantage of Section 48.6416 and buy gasoline tax exempt. It would also place jobbers and refiners on the same competitive basis in serving state and local accounts. Third, the proposed amendment, by allowing wholesale purchasers at the terminal to remit the tax, would enable gasohol blenders to pay the reduced tax rate to IRS directly on those gallons that are blended.

Finally, the change would still provide IRS a clear-cut audit trail to prevent tax evasion. IRS can merely match a wholesale distributor/jobber's purchases at the terminal with the taxes remitted. The only justifiable allowance for not remitting taxes on every gallon purchased would be for sales to state and local governments and the reduced tax rate applicable to gasohol. Moreover, the bonding and reporting requirements would be a significant deterrent to evasion.

This proposed amendment, sponsored by Rep. J. J. Pickle (D-TX), was adopted by the House of Representatives as part of the Omnibus Budget Reconciliation Act on October 29, 1987, but was dropped in conference

along with other provisions of that bill which did not increase revenue to the federal government. This was consistent with the White House - Congressional Budget Summit agreement of November 18, 1987.

Diesel Excise Tax Collection Process: Congressional Action Forces Industry Change

As part of the Omnibus Budget Reconciliation Act of 1987 (PL 100-203), Congress changed the collection procedure for the 15.1 cents per gallon federal diesel fuel excise tax. This section of the law is schedule to take affect April 1, 1988. Under Section 10502 of that Act, the diesel fuel excise tax will be collected by the "producer". The term "producer" is defined to include refiners, terminal operators, and wholesale distributors who register, report, and post a bond as required by the Internal Revenue Service (IRS). All current tax exempt purchasers including farmers, drilling contractors, marinas, and other off-road users must, effective April 1 of this year, begin paying the tax and applying for a refund or credit from the IRS. In addition, all retailers who currently have the right to pay the tax to the IRS must also pay it to their refiner or wholesale distributor. Residential home heating oil is exempt from the tax.

The Department of Treasury has the discretion to exempt other users from payment of the tax including state and local governments, diesel fuel used in trains, taxable fuels used for industrial use other than as a motor fuel, and commercial aviation fuel.

Prior to this change, diesel fuel excise taxes were considered a retail tax. The tax was paid to the government by the retailer or end user. However, Congress, as part of the Tax Reform Act of 1986, enacted a procedure whereby a wholesale distributor and retail dealer could mutually agree to have the wholesale distributor collect and remit the diesel fuel excise taxes.

Diesel Excise Tax Collection Process: IRS Inaction Thwarts Congressional Intent

All of the problems with this new collection procedure are not yet known. IRS on March 3 issued an advanced notice on how the procedure may work. This document is not the final word; rather it is meant to provide interim guidance prior to the issuance of proposed regulations. The notice will not even appear in the Federal Register and will not be included in an IRS Bulletin until March 28, 1988. This

is not the first time, however, IRS has failed to issue timely regulations in compliance with Congressional directives. I would invite the Subcommittee's attention to two recent examples. First, on March 1, IRS released a seven page notice of proposed rulemaking relative to the change mentioned earlier that was incorporated in the Tax Reform Act 1986. That law was signed on October 22, 1986. However, it took over sixteen months to issue "proposed temporary regulations".

These proposed regulations are to be effective and applied to sales of diesel fuel for use in diesel-powered highway vehicles made after March 31, 1987, and before April 1, 1988. In other words, it took IRS well over a year to come out with regulations that can now only be effective for one month, March 1988, because Congress has subsequently passed another law which will change the diesel excise tax collection procedure as of April 1, 1988!

As a second example, IRS did not come out with their proposed regulations on the changes in the gasoline excise tax collection procedure until November 18, 1987, more than a year after the Tax Reform Act of 1986 was signed into law. In its November 18 notice, IRS solicited public comments until December 18, and then, in the best example of all, had a public hearing on January 5, 1988, four days after the new procedure was scheduled to take effect. Since then, at least six different "notices" have been issued to correct errors and clarify confusing passages of the proposed regulations. However, some errors, such as a section that disallows credits or refunds of the LUST tax to state and local governments and hospitals, still remain uncorrected.

Mr. Chairman, the marketers PMAA represents and I believe the vast majority of participants in this industry want to abide by the law. We have tried to be as cooperative as possible with government efforts to reduce excise tax evasion. But how can we really be expected to comply with the law, Mr. Chairman, when we are constantly being barraged with conflicting information and last minute changes in the rules coming out of Washington? For instance, the Nebraska IRS District Office is apparently telling marketers that they will all be required to post bonds even though the March 3 IRS guidance document relative to diesel fuel states that such bonds will not be required in cases where marketers have good federal tax payment histories.

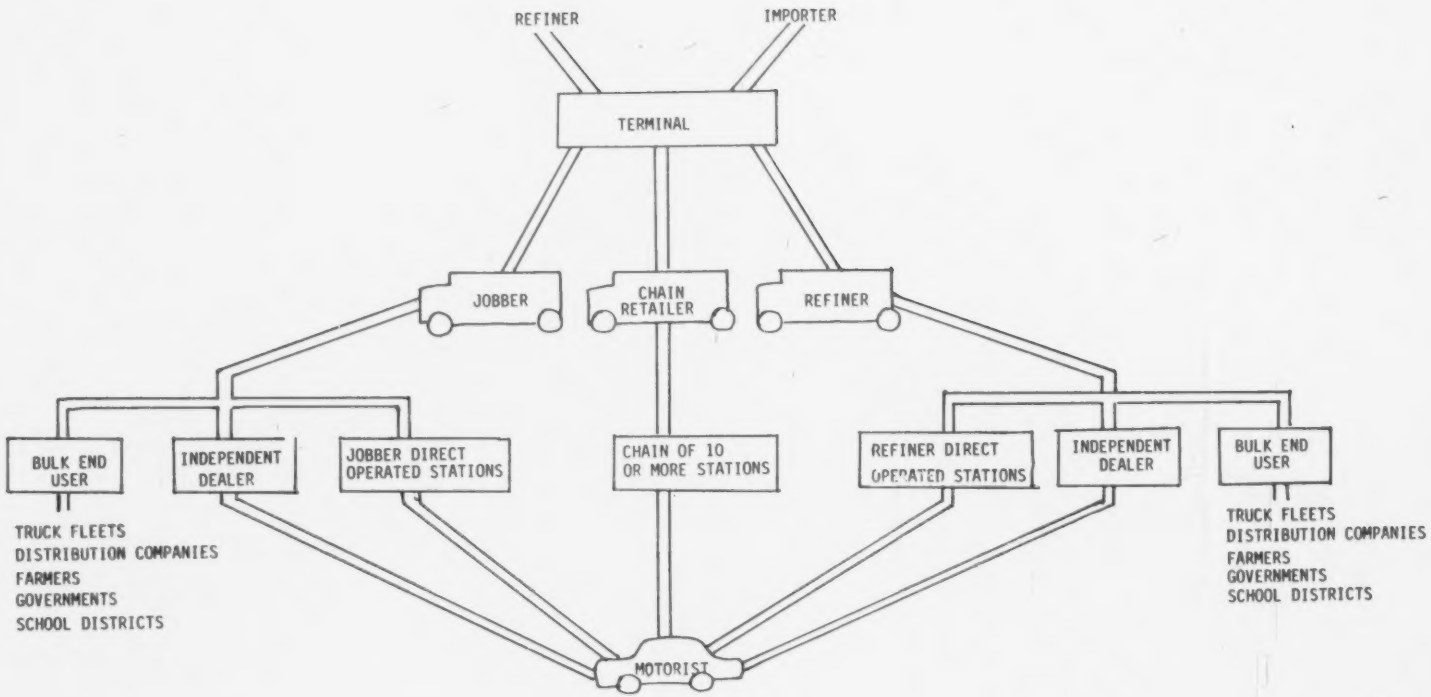
Conclusions

Mr. Chairman, the Petroleum Marketers Association of America would again like to commend you for holding his hearing. The federal gasoline and diesel excise tax collection issues are important, and they need to be addressed expeditiously and comprehensively.

In conclusion, PMAA hopes that Congress will address the gasoline and diesel Federal excise tax issues in a comprehensive way. Both issues are directly interrelated, and PMAA sees no substantive reason for Congress to Act on one and not the other. We believe our testimony today establishes without any doubt the need to act and act quickly. The solutions PMAA is putting forward are reasonable and equitable, and we strongly urge the Finance Committee to adopt these solutions.

Thank you Mr. Chairman and members of the subcommittee. I will be happy to try to respond to any questions you may have.

ATTACHMENT II



PMAA: 8/87

PMAA PETROLEUM MARKETERS ASSOCIATION OF AMERICA
Representing Independent Petroleum Marketers

ATTACHMENT III

GASOLINE/DIESEL FEDERAL EXCISE TAX COLLECTION PROCEDURE
Legislation introduced January 25 through March 10, 1988.

BILL	SPONSOR	COSPONSORS THRU 3/10/88	DATE OF INTRO	COM.	NOTES
			HOUSE		
H.R. 3844	Daub	Dorgan (orig.) 81 total	1/25/88	W&M	Farm Diesel, Gasoline, Gasohol.
H.R. 3850	Jontz	20 orig. 57 total	1/25/88	W&M	Farm Diesel.
H.R. 3865	Combest	23 orig. 114 total	1/27/88	W&M	Farm/Off-road Diesel.
H.R. 3866	de le Garza	29	1/27/88	W&M	Farm/Off-road Diesel.
H.R. 3881	Ms. Smith/NE	19	1/28/88	W&M	Farm Diesel.
H.R. 3892	Neal	72	2/02/88	W&M	State & Local Gov't. Gasoline.
H.R. 3985	Whitten	0	2/22/88	W&M	Farm Diesel, Gasoline, & Gasohol.
H.R. 3989	Inhofe	0	2/24/88	W&M	Farm/Drilling Diesel, State & Local Gov't. Gasoline.
H.R. 3990	Alexander	0	2/24/88	W&M	Farm/State & Local Gov't Diesel, Gasoline.
H.R. 4000	Horton	0	2/24/88	W&M	State & Local Gov't. Diesel.
H.R. 4007	Schuette	2	2/24/88	W&M	Farm Diesel, Farm Gasoline.
H.R. 4117	Lott	0	3/9/88	W&M	Farm/Off-road Diesel
H.R. 4129	Hubbard	0	3/10/88	W&M	Farm Diesel
			SENATE		
S. 2003	Gramm	34	1/25/88	Fin.	Farm Diesel.
S. 2062	Nickles	9	2/17/88	Fin.	State & Local Gov't. Gasoline.
S. 2067	Conrad	1 orig. 2 total	2/17/88	Fin.	Farm Diesel, Gasoline, Gasohol.
S. 2075	Daschle	17	2/19/88	Fin.	Farm Diesel.
S. 2118	Gramm	0	3/2/88	Fin.	Off-road Diesel.
S. 2128	Warner	7	3/3/88	Fin.	Fishing Industry Diesel.

gr:3/15/88

Howell Heflin

TESTIMONY

OF SENATOR HOWELL HEFLIN

ON DIESEL FUEL TAX COLLECTION PROCEDURES

SENATE COMMITTEE ON FINANCE

MARCH 16, 1988

Mr. Chairman, I would like to thank the Finance Committee for providing me with the opportunity to testify today on the diesel fuel collection procedures in the Budget Reconciliation Act. The Budget Reconciliation Act of 1987 changed the collection point for diesel fuel excise tax on federal highway users from retailers to wholesalers. This new tax collection procedure, which is scheduled to take effect April 1, 1988, is intended to strengthen enforcement and to increase the collection of the diesel tax from those who use our nation's highways. These are goals I strongly support. However, the means Congress devised to achieve these ends are inefficient, unwise and unworkable. I therefore call for the speedy repeal of these provisions.

Before this act was passed, a retailer, who was collecting the tax, was presumed to be able to distinguish between sales of fuel to highway and non-highway users. The retailer would then collect the tax due from taxable users of the fuel but would not collect any tax from exempt users. Under the new procedure, diesel wholesalers are responsible for collecting the tax and remitting it to the Internal Revenue Service. Diesel wholesalers will have no idea who the end-user of the fuel will be and thus will have to charge the tax on all sales. This will force virtually all diesel consumers to pay the tax up-front when they purchase fuel. Those who did not use the fuel on a federally-funded highway will have to be apply for a refund from the Internal Revenue Service.

Mr. Chairman, this amounts to an interest free loan by the consumers to the federal government. The unfairness of this situation is blatantly obvious. This will have a profound effect upon all consumers of diesel fuel, such as states, local municipalities, farmers, fishing vessels, the mining industry and the petroleum industry (which is itself a large consumer of diesel fuel).

Although all of these groups will feel the burden of such a severe cash flow drain, perhaps none will feel it as strongly as the American farmer. American agriculture uses over 3 billion gallons of diesel fuel per year. Multiplying this by 15 cents per gallon, we find that the agricultural sector will make a $400 million tax free loan to the Treasury every year. This will be because of a tax they do not even owe. Add to this the regulatory and paperwork burden, and you will see that the impact will be devastating.

Mr. Chairman, the effective date of the revised diesel fuel tax collection procedures is April 1st of this year. I thank the Finance Committee for holding these hearings in a timely manner. I encourage the members of the Committee to quickly mark-up and report out legislation on this matter. I then call for the full Senate to quickly consider and pass this matter before the effective date of this provision.

Thank you, Mr. Chairman.

TESTIMONY OF SENATOR J. BENNETT JOHNSTON
BEFORE THE SENATE COMMITTEE ON FINANCE
MARCH 16, 1988

I am grateful to the Committee for scheduling this hearing to allow the oil and gas industry, farmers, and other off-road diesel fuel consumers to express their concerns about the upcoming change in the Federal diesel fuel tax collection procedures.

By now it is no secret to my colleagues on this Committee that the provision in the Budget Reconciliation Act that changes the collection point of the Federal diesel fuel tax has caused a great deal of commotion among many tax exempt users. In Louisiana alone this new regulation is going to create an administrative nightmare and financial burden for thousands of small businesses. Consequently, yesterday I introduced S. 2168, legislation to allow all off-road users such as oil and gas drilling and service contractors, farmers, shrimpers, fishermen, marine operators, construction contractors, etc. to continue to purchase diesel fuel on a tax free basis. Given the April 1 effective date in the reconciliation bill I urge the Committee to act on S. 2168 as expeditiously as possible.

As I am sure you are aware, over the last couple years Louisiana has been suffering from a severe economic depression. We currently have one of the highest unemployment rates in the nation and our industries cannot afford to suffer any further financial set backs. We are working hard to make our way out of this depression and will continue to do so; however, the change in the collection of Federal diesel fuel tax will add yet another unnecessary hurdle for many individuals and small businesses to get over on the road to economic recovery.

The plight of the domestic oil industry has be one of great concern over the last several years. In order to obtain a healthy and viable oil industry we must do all we can to create incentives to continue production. Requiring oil and gas related firms to pay 15.1 cents per gallon on diesel fuel will only add to the financial hardship of an already strapped industry. I would like to share with you the tremendous burden that this provision will place on that industry.

Currently there are 3,000 oil drilling rigs in the United States that are available to work. Compare that to 1981 when there were 5,500 rigs available. Of the 3,000 that are "alive" only 1,000 -- or 20 percent of the 1981 total -- are currently working, consuming approximately 328 million gallons of diesel fuel. At a rate of 15.1 cents per gallon this means that rig operators will have to pay $49,528,000 in diesel fuel taxes at the time of purchase. In Louisiana there are currently 125 on-shore rigs and 95 off-shore rigs in operation. The average diesel fuel consumption per year for one rig is 280,770 gallons and 612,000 gallons respectively. In essence the oil drilling industry will be lending the Treasury over $49 million dollars per year interest free, of which $14,078,673 will come from Louisiana operations. It is inconceivable to me to imagine where the struggling domestic oil industry will come up with an additional $49 million to pay a tax they do not owe!

Another part of the oil industry that stands to be hit hard by the new Federal diesel fuel tax collection procedures is the well servicing industry. Today we have 6,227 active well servicing rigs. Of these, 54 percent are actually operating. The average service rig consumes 24,960 gallons of diesel fuel per year. This means the immediate diesel excise tax liability for this industry will be $12,675,012 per year. Louisiana has 383 well servicing rigs in operation which will face a total of $1,443,512 in diesel fuel tax expense.

We can also add the geophysical industry to the list of oil and gas related businesses that stand to suffer a financial blow as a result of the new diesel fuel tax collection procedures. The geophysical field crews play a vital role in oil and gas

exploration and rely heavily of diesel fuel for their operation. At present there are 175 land and 30 offshore crews working around the United States. The land crews purchase approximately 1,680,000 gallons of diesel fuel per year while the offshore crews use approximately 21,600,000 gallons per year. Their combined tax liability at the time of purchase would be over $3.5 million. Since close to 15 percent of the land crews and 50 percent of the offshore crews are currently working in Louisiana, the geophysical industry in my state is looking at a yearly diesel fuel tax expense of $1,668,852.

The offshore marine services industry, which services and supplies offshore rigs, is also a heavy user of diesel fuel. By conservative estimates, this industry uses 300 million gallons of diesel fuel per year. If the change in collection procedures of Federal diesel fuel tax goes into effect April 1, the offshore marine services industry will have an increased tax burden of $45,300,000. Since all but 15 percent of these vessels work in the Gulf of Mexico, businesses that operate in and around Louisiana will bear 85 percent - roughly $38,505,000 - of the total diesel fuel taxes paid by this industry.

Another industry that will be directly affected by the diesel fuel tax provision is the tug and barge industry which currently transports 40 percent of our nation's petroleum and petroluem products. These vessels use approximately 1.6 billion gallons of diesel fuel annually. At the current diesel fuel tax rate of 15.1 cents per gallon, the tug and barge industry will pay over $24 million in taxes they do not owe and are currently exempt from. This is going to place the tug and barge industry at a competitive disadvantage with the railroad, their chief competitor. Railroads have already been exempt from paying the diesel tax at the time of purchase and will not have to pass on the extra expense of the tax to their customers.

In addition to this tax, the tug and barge industry is also liable for a 10 cents per gallon tax that goes into the Waterway Trust Fund. This tax, which will gradually increase to 20 cents per gallon in 1995, is used for lock and dam construction. I think it is worth noting that when this committee reconsidered this tax in 1986, you recognized the poor economic condition of the industry and voted to contain future tax increases for as long as possible. Given this decision it does not make sense to now have this industry pay a 15.1 cent tax that it does not owe.

I have been concentrating on some of the industries that are vital to Louisiana and that are suffering from the current depression; however, there is another industry that is also suffering from an economic depression throughout the United States. I, of course, am referring to the farmers. At the national level, current law will restrict this industry's cash flow by $400 million per year, of which $12 million will be borne by farmers in my state. This is not fair, particularly in light of the financial struggles facing rural America.

In conclusion, if this provision is enacted on April 1, it will affect the cash flow of the oil and gas related businesses that I have mentioned by over $140 million per year. This figure does not even begin to measure its effect on other businesses that are important to Louisiana, such as those that engage in farming, shrimping, fishing, forestry, and construction. These industries can ill afford the financial setback that paying diesel fuel tax upfront will create. Therefore, I urge the Committee to act favorably on S. 2168 before this administrative and economic nightmare has a chance to take hold on April 1.

Thank you.

STATEMENT OF
JACK KELSEY
VICE PRESIDENT
NATIONAL FARMERS UNION

Mr. Chairman, my name is Jack Kelsey. I am President of Oklahoma Farmers Union. Last week, I was elected National Vice President for National Farmers Union, a general farm organization of 250,000 farm and ranch families throughout the United States.

We appreciate this opportunity to present the Farmers Union's views on a very important issue of collection of diesel fuel tax. In convention last week, local elected delegates debated and passed the following Special Order of Business unanimously and, I must say, it was probably the number one topic of discussion.

ARTICLE XII
SPECIAL ORDER OF BUSINESS
Adopted by delegates to
the 86th Annual Convention
National Farmers Union
Albuquerque, New Mexico
March 9, 1988

Repeal of Provision Imposing an Excise Tax on Farm Diesel Fuel

Congress must act before April 1, 1988, to assure that U.S. farmers do not become the costly victims of a deficit-reduction ploy in the Budget Reconciliation Act adopted by Congress last December.

That statute imposed a 15-cent a gallon excise tax on farm diesel fuel beginning on April 1, 1988. It was estimated that the tax would raise $420 million in revenue but that it would not cost farmers anything because they could file for a refund later, perhaps when they file their next income tax return.

However, the new tax would require farm operators to pay 20 percent more for their diesel fuel at planting time and then wait several months or perhaps near to a year to obtain a refund.

For many farmers, the imposition of the diesel tax will aggravate cash flow problems which are already serious.

This is a needless $420 million in punishment for U.S. farmers, particularly in view of the fact that no real long-term deficit reduction will be achieved.

The view we express today is shared by National Farmers Organization, American Agricultural Movement, National Save the Family Farm Coalition, and the League of Rural Voters.

The change in the collection point of the diesel tax has, in my opinion, universal opposition of all the farm group representatives with whom I have had the opportunity to talk.

Mr. Chairman, it is very seldom that changes put forth by Congress miss the mark, but this diesel tax collection will, in our opinion, cause great problems and financial stress on all parties concerned.

The small farmer, who is under the greatest financial strain, will be forced to borrow more money to pay a 15-cent per gallon tax on fuel that is used off-road in his normal farming operations. This fuel has historically been exempt from road-use tax, and it is the intent that it will be exempt in the future. However, due to Budget Reconciliation number shuffling, this tax will be collected, then returned to the farmer at some future time. Large fuel buyers will be inconvenienced for as little as 30 days. Small farmers will borrow money and, in effect, lend it to the government interest-free.

At first, it appears the government has a great windfall. In closer analysis, it is obvious that even the government loses when the cost of the paper work is calculated. The added expense of borrowing the money by farmers is tax deductible. Therefore, the U.S. government is the ultimate loser.

It is reasonable to assume that it will not be long before the individual states will decide that early collection is the logical step. What started out as a program to catch a few tax cheats will cost the small family farmer 25 percent more for his farm fuel. The need to borrow more money at a time when he is having trouble repaying what he already owes does not seem to be the way to go.

Mr. Chairman, the American farmer wants to pay his fair share. We are ready to do what is necessary to get our financial house in order. To continue a tax collection program where all parties concerned lose is senseless. We think there is still time for reason to prevail, and the problem can be rectified.

The United States Senate must show that, when mistakes are made, the leadership can and will pass correcting legislation in time to prevent needless problems. Agriculture has had more than its share of difficulty in the past few years.

Mr. Chairman, the Farm Credit Act that was passed with your guidance was a great step towards the recovery of rural America. The correction of the problem in front of us today will also help in that recovery.

We thank you, Mr. Chairman, and would be pleased to attempt to answer any questions.

Testimony By Congressman Trent Lott
before the Senate Finance Subcommittee on
Energy and Agricultural Taxation
March 16, 1988

I am here representing the widespread group of people throughout the State of Mississippi who will be adversely affected by the diesel fuel tax to go into effect on April 1, 1988. I have heard from farmers in Clarksdale, oil service workers in Columbia, contractors in Greenwood, barge operators in Vicksburg, loggers in Hattiesburg and, of course, shrimpers in my district on the Gulf Coast. All of these hard-working business people rely on diesel fuel for their livelihoods.

To these businessmen, diesel fuel represents their blood supply. Noting this, Congress passed a law exempting off-highway diesel fuel users from having to pay a tax on the fuel they need to survive.

All was fine until last December when Congress passed the Omnibus Budget Reconciliation Act of 1987 which included, among who knows what else, a provision requiring those "off-highway business users" to pay the tax on purchase. However, because these users are still considered nontaxable purposes under the law, it will now be necessary for them to apply to Treasury to get their money back.

It makes no sense for the IRS to collect this money, only to turn around and have users who are exempt file for a refund. Granted, farmers may file for quarterly refunds of the tax, but only if the refund for the quarter totals $1,000. What about those who do not total that amount or those who will not have taxable income against which a credit could be applied? This provision is guaranteed to create substantial cash flow problems for all of them. Both the additional time and trouble involved in filing for the rebates and the time it will take for most small farmers and fishermen to receive their refunds impose serious new hardships on these small businessmen.

I am sure you can appreciate the cash flow problems which farmers are already having in these troubled times for the agricultural economy. To now require farmers to wait for up to a year for a refund on taxes paid for a nontaxable purpose will only exacerbate these problems. The same obviously applies to commercial fishermen and others.

As I have stressed, we must do something to correct this obvious inequity. Furthermore, we must do something to help prevent surprises like this from appearing out of the blue in the future. I was appalled that such a controversial provision was haphazardly attached to the Omnibus Budget Reconciliation Act. Nevertheless, how do we proceed from here to attempt to alleviate the hardships being imposed by this new provision?

I have contacted Treasury Secretary James A. Baker; Congressman Dan Rostenkowski, Chairman of the House Committee on Ways and Means, and Congressman John Duncan, Ranking Republican on Ways and Means, to respectfully urge ~~them~~ their expeditious consideration in order to address the problem before the April 1 deadline. In addition, I have introduced a bill to rectify the problem and cosponsored the Farmer Fuel Tax Relief Act (H. R. 3844), introduced by Congressman Hal Daub and a similar bill (H. R. 3865), introduced by Congressman Larry Combest.

Mississippi tow boat operators, farmers, fishermen and many others are upset at Congress over a money maze that's leaving some of them tangled in a financial net. It seems to me that a means can and should be found to restore the previous exemption for these diesel fuel users while still achieving the objective of better compliance and efficiency. Colleagues, it's time to untangle the net.

STATEMENT OF SENATOR FRANK H. MURKOWSKI
OVERSIGHT HEARING
SENATE COMMITTEE ON FINANCE
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
MARCH 16, 1988

IMPACT OF FEDERAL DIESEL FUEL TAX ON OWNERS OF FISHERIES VESSELS.

GOOD MORNING MR. CHAIRMAN, MEMBERS OF THE SUBCOMMITTEE. I AM PLEASED TO HAVE THE OPPORTUNITY TO BE HERE TODAY TO TESTIFY ON A PROBLEM THAT WILL SOON CAUSE AN UNNECESSARY AND UNDUE HARDSHIP TO THE U.S. COMMERCIAL FISHING INDUSTRY.

STARTING THIS APRIL 1 NEARLY ALL OFF-ROAD USERS OF DIESEL FUEL WILL BE REQUIRED TO PAY, FOR THE FIRST TIME, A 15.1 CENTS PER GALLON FEDERAL EXCISE TAX ON DIESEL FUEL. THE OFF-ROAD USERS MAY LATER CLAIM A REFUND, EITHER QUARTERLY OR ANNUALLY FOR THAT PORTION OF TAX PAID ON DIESEL FUEL USED OFF-HIGHWAY.

THESE NEW CHANGES WILL GREATLY HAMPER THE ECONOMIC HEALTH OF OUR U.S. COMMERCIAL FISHING INDUSTRY--AN INDUSTRY THAT RELIES TO A LARGE EXTENT ON TAX-FREE DIESEL FUEL. THAT IS WHY I AM HERE TODAY AND THAT IS WHY I HAVE JOINED WITH SENATOR WARNER AND OTHERS ON A BILL, S.2128, TO PERMIT TAX-FREE SALES OF DIESEL FUEL FOR OFF-ROAD USE BY COMMERCIAL FISHERIES VESSELS.

TRADITIONALLY, FUEL RETAILERS HAVE COLLECTED THE FEDERAL EXCISE TAX ON DIESEL FUEL. THEY DID NOT COLLECT THIS TAX ON SALES INTENDED FOR OFF-HIGHWAY USE, HOWEVER. BECAUSE THE FUEL TAX REVENUES HELP MAINTAIN OUR FEDERAL HIGHWAY SYSTEM, THOSE WHO PURCHASE DIESEL FUEL FOR OFF-HIGHWAY USE --AS YOU MIGHT GUESS OUR COMMERCIAL FISHERMEN DO NOT MAKE GREAT USE OF THE HIGHWAYS WITH THEIR BOATS--HAVE BEEN EXEMPT FROM DIESEL FUEL TAXES.

TO EASE TAX COLLECTION EFFORTS AND ENSURE THAT TAX-EXEMPT FUEL SALES ARE RELATED TO OFF-HIGHWAY USES, LAST YEAR'S BUDGET RECONCILIATION ACT CHANGED THE DIESEL FUEL TAX COLLECTION PROCEDURES. ON APRIL 1 WHOLESALERS OF DIESEL FUEL ARE REQUIRED TO COLLECT THE FEDERAL EXCISE TAX ON ALL SALES OF DIESEL FUEL.

THESE NEW TAX COLLECTION CHANGES WILL CAUSE TREMENDOUS CASH FLOW PROBLEMS FOR DIESEL FUEL WHOLESALERS THAT SELL ON CREDIT.

WHOLESALE FUEL DEALERS MUST OFTEN SELL ON 30 TO 90 DAY CREDIT TERMS. THE NEW CHANGES REQUIRE THAT WHOLESALERS COLLECT AND PAY THE DIESEL FUEL TAXES TO THE IRS WITHIN 1 TO 3 WEEKS OF

THE SALE. AS A RESULT, MANY WHOLESALERS WILL END UP PAYING THOUSANDS OF DOLLARS OF THEIR CUSTOMERS FUEL TAXES BEFORE THEY ARE PAID BY THEIR CUSTOMERS.

IT IS ESTIMATED THAT A TYPICAL WHOLESALE FUEL DEALER IN KODIAK, ALASKA WHO SELLS 500,000 GALLONS OF DIESEL FUEL PER MONTH, WILL HAVE TO PAY APPROXIMATELY $75,000 IN NEW UP-FRONT OUT-OF-POCKET TAX PAYMENTS. IT WOULD COST FUEL DEALERS IN DUTCH HARBOR OUT ON THE ALEUTIAN CHAIN EVEN MORE -- PERHAPS AS MUCH AS $450,000 PER MONTH.

OWNERS OF FISHERIES VESSELS WILL ALSO FACE SEVERE CASH FLOW PROBLEMS AS THEY PAY 15.1 CENTS OF TAX ON EVERY GALLON OF THEIR DIESEL FUEL. ALTHOUGH THEY CAN FILE FOR A REFUND, IT WILL OFTEN TAKE UP TO A YEAR TO RECEIVE IT.

FOR EXAMPLE, AN ALASKAN FISHING FACTORY TRAWLER WILL USE BETWEEN 150,000 AND 450,000 GALLONS OF DIESEL FUEL PER QUARTER. BEGINNING ON APRIL 1, THE OWNERS OF THESE VESSELS WILL HAVE TO PAY FROM $22,500 TO $68,000 EACH QUARTER IN TAXES.

THESE NEW TAX CHANGES COULD NOT HAVE COME AT A WORSE TIME. MANY OF OUR AMERICAN VESSELS ARE STRUGGGLING TO COMPETE AGAINST FOREIGN PRODUCERS THAT OFTEN OPERATE AT MUCH LOWER COSTS. INSTEAD OF USING THEIR MONEY FOR NEEDED BUSINESS EXPENSES, OUR FISHERMEN WILL HAVE TO PAY FOR TAXES THAT WILL BE REFUNDED LATER.

THE NEW TAX CHANGES MAY ALSO AFFECT THE AVAILABILITY OF DIESEL FUEL FROM SMALLER WHOLESALE DEALERS.

UNDER THE NEW LAW WHOLESALERS THAT BUY DIESEL FUEL MUST BE REGISTERED AND BONDED TO AVOID PAYING A DIESEL FUEL TAX. BONDING MAYBE DIFFICULT FOR SOME TO GET, AND EVEN IF SO, IT WILL CERTAINLY CREATE AN ADDED BUSINESS EXPENSE, AND POSSIBLE INCREASED CUSTOMER DIESEL FUEL PRICES. I MIGHT ADD AT THIS MOMENT BONDING INSURANCE COMPANIES ARE STILL AWAITING LANGUAGE FROM THE IRS THAT WILL ENABLE THEM TO BOND WHOLSESALE DIESEL FUEL DEALERS.

FINALLY, I AM NOT SURE THAT THESE CHANGES ARE NEEDED TO PREVENT TAX EVASION BECAUSE I DOUBT WHETHER SUCH TAX EVASION IS OCCURRING IN THE COMMERCIAL FISHING INDUSTRY -- ESPECIALLY IN MY OWN HOME STATE, WHERE DIESEL FUEL IS USED IN SUCH REMOTE AREAS AS THE BERING SEA AND GULF OF ALASKA, AND ROADS ARE VIRTUALLY NONEXISTENT.

UNDER THE NEW LAW TAX-FREE SALES ARE PERMITTED WHERE DIESEL FUEL IS SOLD FOR USE AS HEATING OIL, AND IN CASES WHERE THE IRS DETERMINES THAT THE DIESEL FUEL IS DESTINED FOR A NONTAXABLE OFF-HIGHWAY USE. FUELS SOLD FOR USE IN DIESEL-POWERED TRAINS, COMMERCIAL AIRCRAFT, INDUSTRIAL PLANTS, AND TO GOVERNEMENT ENTITIES ARE TAX-EXEMPT. I BELIEVE THAT THIS SHOULD AT THE VERY LEAST BE EXPANDED TO INCLUDE FUEL SOLD FOR USE IN FISHERIES VESSELS.

ONE WOULD BE HARD-PRESSED TO SHOW THAT SALES TO FISHERMEN WOULD NOT BE FOR OTHER THAN AN OFF-HIGHWAY USE. AN EXEMPTION FOR SUCH SALES WOULD GO A LONG WAY TO HELP THE OWNERS OF SOME 130,000 FISHING VESSELS IN THE U.S., AND 10,000 OWNERS OF MORE THAN 16,000 REGISTERED COMMERCIAL FISHING VESSELS IN ALASKA.

I AM CONFIDENT THAT WHEN THIS SUBCOMMITTEE IS THROUGH, IT WILL FIND THAT DIESEL FUEL TAX EVASION IS NOT A PROBLEM IN THE COMMERCIAL FISHING INDUSTRY. I BELIEVE THAT IT WILL ALSO RECOGNIZE THE HARDSHIP AND FOLLY IN ASKING PEOPLE TO PAY A TAX THEY DO NOT OWE OR TO EXEMPT THEM FROM A TAX THEY MUST PAY.

MR. CHAIRMAN, I UNDERSTAND THAT YOUR SUBCOMMITTEE'S CHIEF CONCERN IS THE IMPACT OF THE NEW TAX COLLECTION PROCEDURES ON AMERICA'S FARMERS. I ASK THAT YOU RECOMMEND LEGISLATION WHICH WILL NOT ONLY AID FARMERS, BUT WILL HELP THE COMMERCIAL FISHING INDUSTRY AS WELL. LIKE AGRICULTURE, IT IS AN INDUSTRY THAT CAN ILL-AFFORD ADDITIONAL UP-FRONT EXPENSES.

TESTIMONY OF SENATOR DON NICKLES
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
MARCH 16, 1988

Mr. Chairman, the legislation I have introduced in regard to federal motor fuel tax exemptions for state and local governments and other groups is necessary to alleviate an unfair tax burden placed upon them by provisions in the Tax Reform Act of 1986 and the Budget Reconciliation Act of 1987.

S. 2062 removes the burden placed on state and local governments that they pay the federal gasoline excise tax at the time of purchase and returns it to the historic system allowing them to claim an exemption at the time of purchase. This requirement was mandated in the Tax Reform Act of 1986 and went into effect January 1, 1988.

The new law forces state and local governments to file the proper paperwork with the IRS in order to be eligible for a rebate on the gasoline tax they paid. This rebate can take as long as a year to receive, while the IRS collects and keeps the interest on the state and local tax payments.

The costs that state and local governments have to absorb include: costs associated with record keeping and filing for a rebate, absence of funds while the IRS conducts an audit on the paperwork, and loss of the interest earned on their money which the IRS keeps.

While the state and local governments are incurring the costs of the rebate process, the IRS is also incurring its own set of administrative costs in processing the paperwork from thousands of state and local governments. At present, there is no available estimate on the administrative costs to the IRS, but the increase in paperwork generated by the rebate process will likely raise their operational costs substantially. Any revenue that might emerge from this new collection system does not justify the burdensome manner by which it was collected.

Let me give you some examples of what this will cost in my own state of Oklahoma. The State of Oklahoma spends $6.2 million a year for gasoline bringing its total tax liability under the new law to $771,023. Other examples include:

--Tulsa	$158,528 a year in tax liability
--Oklahoma City	144,872
--Muskogee	30,000
--Moore	13,500

--Ponca City	12,870
--Duncan	11,700
--McAlester	9,000
--Guymon	6,840
--Grove	1,440

The Chairman of the Oklahoma Association of Local Governments, Gale Humble, wrote to me urging repeal of this new system. He wrote, "This will result in taxpayers receiving fewer services or paying more taxes solely because of an administrative regulation."

Recently the IRS has been sympathetic to the objections of state and local governments regarding the collection of the diesel fuel excise tax. Using the discretion allowed them in the Budget Reconciliation Act of 1987, the IRS has issued regulations that permit state and local governments to claim exempt status at the time of their diesel fuel purchase, thereby avoiding payment of the diesel fuel excise taxes altogether.

However, the Tax Reform Act of 1986 did not provide the Secretary with the same discretion with respect to the motor gasoline excise tax. Within the more narrow discretion available to it under the Tax Reform Act of 1986, the Service released Notice 88-13 on January 28, 1988. This notice clarified that IRC section 6416 still permits state and local governments to buy gasoline without having to pay the federal excise tax at the time of purchase if certain conditions are met. Those conditions require that all parties in the distribution chain selling to the state or local government must agree to use the IRC 6416 procedure, which involves not collecting the tax from the subsequent seller so long as the ultimate purchaser of the gasoline uses the fuel for exempt purposes.

Very simply, this so-called simplifying provision is really nothing of the sort. Reliance on section 6416 is not sufficient to resolve the economic hardship imposed on smaller local governments. S. 2062 would remove the reliance on section 6416, and eliminate the hit or miss results and potential for unfair price discrimination.

I would now like to make a few comments on the comprehensive bill that Senator Dixon and I will introduce today, the Motor Fuels Excise Tax Relief Act of 1988. This bill would return to traditionally exempt taxpayers the opportunity to again purchase on a tax-free basis. This bill would change the gasoline tax collection requirements with respect to nonprofit educational organizations as well as state and local governments. The bill also reinstates the tax-free status on diesel fuel purchases by all "off-highway

business" users as defined in IRC section 6421. This would change the collection point not only for farmers but also for diesel used for commercial fishing boats, and for oil field equipment.

Finally, this bill includes provisions modifying the excise tax collection rules to permit gasohol blenders to pay the lower tax rate for gasohol even if they blend the fuel after leaving the terminal; and to permit wholesale distributors to remit the gasoline tax directly to the Treasury.

One last point I would like to make is concerning the effect that the new diesel excise tax laws are going to have on the farming industry if they are not rescinded prior to their effective date of April 1, 1988.

On January 27, I cosponsored legislation with Senator Gramm (S. 2003) which would restore to farmers their exemption from paying the diesel fuel excise tax at the time they make their fuel purchase. And as I previously mentioned, this provision for farmers is also included in the comprehensive bill that Senator Dixon and I will introduce today.

The new diesel tax law that takes effect April 1 will have a a harsh impact on an already weakened industry. According to Oklahoma Agriculture Statistics of 1986 and our most recently compiled data, the average wheat farm in Oklahoma would be incurring $900 a year in diesel fuel excise taxes. Farmers would then have to apply for a rebate from the IRS by proving that all of the diesel bought at wholesale was used for farm related purposes.

Again, this creates an unfair and unnecessary burden on these farmers while the IRS collects the interest on their tax payments. I believe it is of the utmost importance for Congress to act swiftly in restoring the proper exemptions to certain traditionally exempt groups.

SENATOR PRYOR'S STATEMENT

ON DIESEL AND GAS EXCISE TAX COLLECTION

Mr. Chairman, I want to thank you for holding this hearing today. I have just returned from a week in my home state of Arkansas, and I can truthfully say that very few people were talking about Super Tuesday or relations with the Soviets. During my town meetings across rural Arkansas, what people wanted to talk about most was the collection of federal excise taxes.

In farming communities, farmers explained to me how this new rule would affect their cash flow, in times when the direction of that flow is mostly out. In north east Arkansas, lumbermen described the hardship of lost cash flow and the additional paperwork burden. Likewise, the barge operators of West Memphis and the oil drillers of Smackover could not believe that the federal government would be short-sighted enough to require them to pay taxes not actually owed and then ask for a refund.

I can also tell this Subcommittee, that although this provision was sold to us as being "O.K." for the oil jobbers, the small jobbers of my state are going to suffer considerably by the implementation of this provision. Many of these jobbers advance

diesel fuel to farmers and do not demand payment until the crops are harvested. In effect, under this rule they would then be carrying the "float."

Finally, Mr. Chairman, the Finance Committee needs to address the issue of gas excise collection for local and state governments. Like the diesel issue, the federal government is hurting groups that can least afford it. In these times of lost revenue sharing, it makes little or no sense to require local governments to give the federal government an interest-free loan.

I am pleased to see that the Chairman of the Finance Committee is taking early action on the issue of diesel excise collection during this Friday's mark-up. I hope that we can move equally as fast on the gas excise tax problem. Once again, I want to thank the the distinguished Senator from Oklahoma for holding this important hearing today.

STATEMENT OF
DENNIS E. ROSS
DEPUTY ASSISTANT SECRETARY (TAX POLICY)
DEPARTMENT OF THE TREASURY
BEFORE THE
SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
COMMITTEE ON FINANCE
UNITED STATES SENATE

Mr. Chairman and Members of the Subcommittee:

I am pleased to have this opportunity to present the views of the Treasury Department regarding possible changes in the collection procedures for the Federal excise taxes on gasoline, diesel, and aviation fuel. Recent legislation has shifted the point at which these taxes are collected to a higher level in the distribution chain -- from the wholesale to the bulk storage terminal level in the case of gasoline and from the retail to the wholesale level in the case of diesel and aviation fuels. In each case, the change was made in order to address serious tax evasion problems by reducing the number of taxpayers permitted to make purchases on a tax-free basis. We believe these changes, which mirror changes that a number of States have made to improve collection of their own fuel excise taxes, will prove highly successful in addressing evasion of Federal excise taxes. We recognize, however, that the changes have raised collateral problems for consumers that use fuel for tax-exempt purposes.

My testimony today will first describe the collection procedures for the excise taxes on gasoline, diesel, and aviation fuel and discuss the reason for the recent amendment of these procedures. Second, I will describe the treatment under the amended collection procedures of persons using fuel for tax-exempt purposes. Third, I will describe several proposals that have been made to revise further these collection procedures. Finally, I will discuss the Treasury Department's views regarding these proposals.

I. Excise Tax Collection Procedures

A. Gasoline Excise Tax

In fiscal year 1987, Federal gasoline excise tax receipts (after refunds) were approximately $9.1 billion. The excise tax rate is 9.1 cents per gallon of gasoline. Of this amount, 9 cents per gallon is transferred to the Highway Trust Fund,1/ with the remaining 0.1 cents per gallon transferred to the Leaking Underground Storage Tank Trust Fund. Certain uses of gasoline are fully exempt from the tax, including export, use by State and local governments, use on a farm for farming purposes, certain other off-highway uses, use in certain buses, and use by nonprofit educational organizations. Other uses are partially exempt from the tax, including use in gasohol, which is taxed at the reduced rate of 3.1 cents per gallon.

Prior to January 1, 1988, the Federal gasoline excise tax generally was imposed on the wholesale dealer at the time gasoline was sold to a retail dealer or, in some cases, to the ultimate consumer. Wholesalers and other persons above the retail dealer level were entitled to purchase gasoline on a tax-free basis, provided they were registered with the Internal Revenue Service. Under this collection system, approximately 12,000 persons were registered with the Internal Revenue Service as eligible to purchase gasoline on a tax-free basis.2/

There was clear evidence of widespread tax evasion under these procedures. This tax evasion generally resulted from

persons registered as wholesalers selling gasoline at a price that included the tax, but failing to remit the tax to the Federal Government. There was substantial evidence of involvement by organized crime in such evasion schemes. The Treasury Department has estimated that the Federal Government was losing approximately $250 million per year from evasion of the excise tax.

In response to this tax evasion problem, the Tax Reform Act of 1986 (the "1986 Act") shifted the collection point for the tax upstream to the point of removal or sale of gasoline by the refiner, importer, or terminal operator. The statute permits refiners and importers to make bulk transfers of gasoline to registered terminal operators without payment of tax. Thus, the general effect of this change is to impose the Federal excise tax at the point the gasoline leaves a bulk storage terminal. The change in the collection system was effective on January 1, 1988.

B. Diesel and Aviation Fuel Excise Taxes

The Federal excise tax on the sale of any liquid as a fuel for use in a diesel-powered highway vehicle is 15.1 cents per gallon and the tax on any liquid (other than any liquid subject to the gasoline excise tax) sold for use as a fuel in an aircraft in noncommercial aviation is 14.1 cents per gallon. Of these amounts, 15 cents per gallon of the diesel fuel tax is transferred to the Highway Trust Fund and 14 cents per gallon of the aviation fuel tax is transferred to the Airport and Airway Trust Fund; the remaining 0.1 cents per gallon of each tax is transferred to the Leaking Underground Storage Tank Trust Fund. Certain uses of diesel and aviation fuel are exempt from these taxes. Exempt uses include export, use by State and local governments, use on a farm for farming purposes, other off-highway uses, use in certain buses, and use by nonprofit educational organizations. In fiscal year 1987, excise tax receipts from the diesel and aviation fuel taxes were $2.7 billion and $0.1 billion, respectively.

Currently, the Federal diesel and aviation fuel excise taxes are imposed on the seller at the time the fuel is sold to the ultimate consumer. Imposing the tax at the retail level maximizes the number of persons involved in collecting the tax. It correspondingly reduces compliance by fostering inefficient tax collection procedures and encouraging development of tax avoidance schemes.

In response to concerns regarding noncompliance, the Omnibus Budget Reconciliation Act of 1987 (the "1987 Act") shifted the point of collection of the diesel and aviation fuel taxes from the retail to the wholesale level. Under the provisions of the 1987 Act, which are effective April 1, 1988, the tax will generally be imposed on the wholesale dealer at the time the fuel is sold to a retail dealer or, in some cases, to the ultimate consumer. Wholesalers and other persons above the retail dealer level will be entitled to purchase diesel and aviation fuels on a tax-free basis, provided they are registered with, and satisfy bonding requirements of, the Internal Revenue Service.

C. Reasons for the Changes in Collection Procedures

Movement of the collection point upstream for both gasoline and diesel fuel has a number of positive compliance effects. First, it results in a shorter audit trail by reducing the number of times that a particular volume of fuel changes hands between the time the fuel is produced and the time the tax is imposed. Second, it reduces the number of transactions on which the tax is imposed, while increasing the average volume of fuel per transaction. Third, it reduces the number of persons that are eligible to purchase fuel tax-free and then remit the tax to the Federal Government. In the case of the gasoline excise tax, moving the collection point to the point at which gasoline leaves the terminal is expected to reduce the number of persons remitting the tax from approximately 8,000 to an estimated 1,000. In the case of the diesel fuel excise tax, moving the collection point to the wholesale level is expected to reduce the number of persons remitting the tax from approximately 60,000 to an estimated 8,000. Finally, taxpayers at a higher level in the distribution chain can be expected, on average, to be financially sounder and maintain better records of their transactions than persons at a lower level in the distribution chain.

Under these new collection systems, the Internal Revenue Service anticipates auditing a much higher percentage of taxpayers and transactions, and doing so at a lower cost, than was previously possible. In the case of the gasoline excise tax, for example, the Service examined only 7.1 percent of the fiscal 1986 returns showing gasoline excise tax liability. Such examinations yielded a total of $36 million in proposed adjustments and penalties. Also in fiscal 1986, the Service examined only 1.7 percent of the diesel tax returns, and recommended additional tax on 84 percent of the examined returns. Although we do not yet know exactly how many excise tax returns will be filed for 1988 under the new collection procedures, we expect that the number will be substantially less, and the percentage examined much greater, than under prior law. In addition, the Service should be better able to collect any deficiencies that it discovers, given the concentration of liability in a smaller number of taxpayers.

As a consequence of the above changes, we expect dramatic reductions in the amount of revenue lost to the Federal Government through excise tax evasion. The Treasury Department estimates that the change in the gasoline tax collection procedures will increase revenues from this tax by approximately $300 million in fiscal 1988, and by approximately $200 million per year in fiscal 1989 through 1993. In the case of diesel and aviation fuels, the new collection procedures are expected to increase revenues by approximately $350 million in fiscal 1988, by approximately $250 million in fiscal 1989, and by approximately $200 million per year in fiscal 1990 through 1993.3/

II. Treatment of Exempt Users

A. In General

Although movement of the excise tax collection point higher in the distribution chain produces important tax compliance benefits, it also creates certain problems for tax-exempt users. In particular, it is often impossible to identify, at the time the tax is imposed, whether the product ultimately will be used for a taxable or nontaxable purpose. Consequently, consumers using fuel for nontaxable purposes may be forced to purchase the fuel at a price that includes the excise tax. As noted earlier, for both gasoline and diesel fuel, nontaxable purposes include export, use by State and local governments, and farming use. In the case of diesel fuel, the largest nontaxable use is as heating

oil -- distillate used for home heating, commercial, and industrial burner units is essentially the same product as diesel fuel used in highway vehicles. Indeed, less than half of all diesel fuel usable in a diesel-powered highway vehicle will, in fact, be consumed in a taxable use. This greater use of diesel fuel for nontaxable purposes explains why the diesel excise tax is imposed at a lower level in the distribution chain than the gasoline excise tax.

Nontaxable users that purchase gasoline, diesel, or aviation fuel at a price that includes the Federal excise tax are entitled to a refund of the tax. Such refunds, however, generally cannot be claimed more often than once annually (quarterly claims may be made if the refund of the tax for the quarter is at least $1,000), and no interest is paid on such refunds. This is obviously an imperfect procedure, since it imposes a tax that ultimately will be refunded, and imposes paperwork and cash flow burdens.

B. Exempt Uses and the Gasoline Excise Tax

By moving the collection point of the gasoline excise tax above the level at which exempt users typically purchase gasoline, the 1986 Act changes may effectively require such users to buy gasoline tax-paid and then apply for a refund. This change has had a particular effect on State and local governments, since they were generally able to buy gasoline tax-free under the prior collection procedures. Under these prior rules, wholesalers and chain retailers were themselves permitted to purchase gasoline free of tax, and no tax was imposed on their sales to State and local governments. Under the procedures now in effect, however, the tax is imposed on the removal of the gasoline from a terminal, which typically occurs before the sale to the State or local government.

As indicated earlier, State and local governments that purchase gasoline at a price that includes the Federal excise tax may obtain a refund of the tax. An alternative procedure is provided under section 6416 of the Internal Revenue Code whereby a State or local government or other exempt person specified in that section can gain the benefit of its exemption. Under the section 6416 procedure, tax paid on gasoline that ultimately is used by a State or local government or other specified exempt person can be refunded to the person that remitted the tax to the Federal Government. A refund is allowed under section 6416 only if the burden of the tax was not, in fact, borne by the exempt person that ultimately purchased the gasoline. Thus, to receive a refund, the taxpayer either must not include the tax in the price at which it sells the gasoline or must agree to repay the amount of the tax to the person that ultimately sold the gasoline to the exempt person.

Although the section 6416 procedure is preferable to the refund procedure from the standpoint of State and local governments, it is not a completely satisfactory solution. State and local governments have no legal right to buy tax-free under section 6416; whether they can do so depends on their bargaining power relative to that of their suppliers. In addition, like the procedure allowing a refund directly to the government, it does not avoid imposition of a tax that later will be refunded; it merely shifts the paperwork burden and loss of cash flow. The loss of cash flow is, however, significantly less than under the direct refund procedure since a taxpayer obtaining a refund under section 6416 may credit the refund against the payments due on its next excise tax return.

It should be noted that many of the problems experienced by State and local governments in adjusting to the new procedures may be transitional. Many State and local governments did not become aware of the new collection procedures until they took

effect on January 1. Therefore, these governments did not take steps to prepare for the new procedures in advance, such as persuading their suppliers to sell tax-free under the section 6416 procedure, anticipating the effect of the new procedures in their 1988 budgets, and setting up administrative procedures to claim refunds. Thus, we expect that many of the problems experienced by State and local governments with the new procedures may diminish as time passes.

C. Exempt Uses and the Diesel and Aviation Fuel Excise Taxes

The 1987 Act amendments to the diesel and aviation fuel tax collection procedures permit tax-free purchases of fuel for five specified categories of non-taxable uses: use as heating oil; use in a diesel-powered train; use in an aircraft in commercial aviation; use other than as a motor fuel; and use by a State or local government. Persons purchasing fuel for such uses were viewed as typically making large purchases at the wholesale level and as relatively unlikely to be involved in tax-avoidance schemes. Even for these categories of uses, tax-free purchases are permitted only to the extent authorized in Treasury regulations.4/

Under the 1987 Act, no regulatory authority exists to permit other persons to make tax-free purchases of diesel fuel. As under prior law, persons purchasing diesel fuel for certain other purposes, including use on a farm for farming purposes, use in commercial fishing vessels, and non-vehicle use (e.g., in stationary motors), are exempt from tax. Such persons must, however, purchase the fuel at a price that includes the tax and then file for refund of the tax. The inability to obtain an up-front exemption applies even if the fuel was purchased from a wholesaler, and thus no tax was imposed prior to the sale to the person using the fuel for an exempt purpose.

Moreover, in the case of diesel and aviation fuels (unlike gasoline), neither section 6416 nor any other procedure is available whereby the exempt user may purchase the fuel tax-free, with a refund allowed to the person that remits the tax. Rather, the 1987 Act permits only the exempt user to make a refund claim.

As members of Congress are well aware, the agriculture community has been particularly concerned about the change in the collection point of the diesel fuel tax. Farmers are not included among the categories of exempt users permitted to make tax-free purchases. The resulting requirement that farmers purchase diesel fuel at a price that includes the excise tax and then seek a refund has the effect of increasing the costs of doing business for a group already experiencing cash flow problems.5/ Data from a 1982 Department of Agriculture census suggests that the amount of diesel fuel tax that would be borne by the average farmer, and subsequently refunded, would be approximately $340 per year. The fact that farmers generally do not pay estimated income tax increases the burden of the new diesel tax collection procedures. Taxpayers who pay estimated tax and are entitled to a refund of the diesel excise tax can reduce the amount of their estimated tax payments by the refund. Farmers, however, will have to wait for the government to process their refund claims.

While we recognize this cash-flow burden, it may be noted that most farmers have had to follow similar procedures with respect to the excise tax on gasoline, which has always been collected above the retail level and for which no up-front exemption has been allowed.6/ In 1987, farmers filed 800,000 gasoline tax refund claims, aggregating $117 million. While we realize that farmers now use greater quantities of diesel fuel than gasoline, this has not always been the case. Until recently, approximately equal quantities of gasoline and diesel fuel were used for farming purposes. Farmers have been able to

operate under the refund system in the case of gasoline. Thus, to some extent, it may be the transition from procedures to which farmers have become accustomed, rather than the new procedures themselves, that poses the most serious problem.

III. Proposals To Revise Collection Procedures

A. Gasoline Excise Tax Collection Procedures

Since the 1986 Act was passed, two proposals have been offered to Congress that would further change the collection point of the gasoline excise tax. First, S. 2067 would permit gasoline wholesalers to buy gasoline on a tax-free basis and then remit the tax to the Federal Government (at the time that the seller otherwise would be required to do so). A similar provision was included in H.R. 3545, as initially passed by the House of Representatives last year, but was not ultimately enacted. Second, a proposal to move the tax collection point further upstream was described in a pamphlet on possible options to increase revenues prepared by the Staff of the Joint Committee on Taxation in June 1987 for the Committee on Ways and Means. Under the latter proposal, the tax would be imposed on removal of gasoline from a refinery or from the first storage point in United States customs custody. This proposal is similar to one recently adopted by New York State to address serious problems with evasion of its State gasoline excise tax.

In addition to proposals to change the point of collection, proposals have also been made to provide an up-front exemption from tax on gasoline destined for use by State or local governments or by farmers. For example, S. 2062 (relating to State and local governments) and S. 2067 (relating to farmers) would exempt otherwise taxable sales of gasoline if the purchaser certifies that the gasoline ultimately will be used for these exempt purposes. An important issue under any such "destination" rule is whether the person making the certification would be required to sell directly to the exempt user, or, alternatively, could sell to an intermediary that makes a similar certification. In the latter case, the Internal Revenue Service might be required to examine a chain of certifications in order to trace gasoline to an exempt user. Although the intent of S. 2062 and S. 2067 is not clear, we interpret the language of these bills as requiring that the purchaser sell directly to the exempt consumer.

B. Diesel Fuel Excise Tax Collection Procedures

Numerous bills have been introduced that would add farmers to the categories of exempt persons permitted to make tax-free purchases of diesel fuel. Some proposals, such as S. 2075, would authorize Treasury to permit farmers to make tax-free purchases on the same terms as categories of purchasers currently exempted. S. 2075 would also require that regulations applicable to exempt users be issued no later than 30 days after enactment and would provide a special refund procedure for exempt users who paid tax before issuance of the regulations. Other proposals, such as S. 2067, would permit farmers to make tax-free purchases of diesel fuel at the retail as well as the wholesale level.7/ Another proposal, S. 2003, would require that, under regulations, sales of diesel fuel for farm use be tax-free.

Other proposals would expand further the categories of persons permitted to make tax-free purchases. S. 2128, for example, would extend this privilege to purchasers of diesel fuel, at either the wholesale or retail level, for use in commercial fishing. S. 2118 would extend the privilege to all purchasers of diesel fuel, at either the wholesale or retail level, for off-highway use.

IV. Discussion

A. Gasoline Excise Tax Collection Procedures

The Treasury Department does not support proposals to change the point at which the gasoline excise tax is collected. In particular, the Treasury Department opposes the provision in S. 2067 that would permit gasoline wholesalers to buy gasoline free of tax. We believe that such a change, by substantially increasing the number of persons permitted to buy gasoline on a tax-free basis, would increase opportunities for evasion and would partially defeat Congress' purpose in enacting the changes included in the Tax Reform Act of 1986. We do not believe that imposition of financial responsibility requirements on wholesalers, as proposed by S. 2067, would adequately address these concerns. The Treasury Department estimated that enactment of a similar provision in H.R. 3545, as initially passed by the House of Representatives, would have reduced revenues by at least $39 million in fiscal 1988 and $60 million in each subsequent year through fiscal 1992.

Adoption of the proposal to move the collection point of the gasoline excise tax further upstream, on the other hand, would increase revenues, principally by further reducing opportunities for tax evasion. We believe, however, that the amount of revenue gained by this proposal would be far less than the amount gained by the changes included in the 1986 Act; we expect that these changes will eliminate about 80 percent of the evasion that occurred under the pre-1988 procedures. In addition, movement of the collection point further upstream would exacerbate not only the problems of exempt users, but also problems related to petroleum products and chemicals, such as octane enhancers, that are added to gasoline at lower levels in the distribution chain.8/ For these reasons, the Treasury Department does not advocate moving the collection point for the gasoline excise tax further upstream at this time.

The Treasury Department has serious reservations regarding proposals, such as S. 2062 and S. 2067, that would exempt from tax sales of gasoline destined for use by a State or local government or farmer. Such proposals would inevitably create opportunities for tax evasion that the 1986 Act was intended to close. This is particularly true of any approach that would exempt from tax all sales of gasoline certified by the purchaser to be destined for non-taxable use. We believe that such an approach would exempt much gasoline that ultimately will be used for a taxable purpose. Because many State and local governments and farmers may purchase gasoline more than one step in the distribution chain below the point at which the initial certification would be given, diversion of untaxed gasoline to a taxable use may occur even if the person making the initial certification is acting in good faith.

Some of our concerns with certification proposals would be addressed, at least in part, if an up-front exemption is allowed only for sales to persons that will resell directly to an exempt user, and if the purchaser is required to include with the certification evidence of a specific purchase order from an exempt user. It should be recognized that this approach would not help those exempt users purchasing gasoline more than one level in the distribution chain below the point at which the tax is imposed, since their suppliers could not make tax-free purchases under this approach.

B. Diesel Fuel Excise Tax Collection Procedures

The Administration has under review proposals, such as S. 2075, that would extend regulatory authority to permit tax-free purchases by farmers. If such a provision were to become law, the Treasury Department would, of course, implement the provisions as soon as possible. We believe, however, that the

requirement in S. 2075 that regulations be issued within 30 days after enactment of such a provision imposes an unreasonable deadline. Also, because of the potential for evasion, we would not support permitting farmers or other exempt users to make tax-free purchases at the retail level, as proposed by S. 2067, S. 2128, and S. 2118. Moreover, we believe that the privilege of making tax-free purchases should be subject to such conditions (e.g., registration and satisfactory compliance history) as the Treasury Department may require. Thus, we do not support S. 2003.

The Treasury Department estimates that the revenue impact of permitting tax-free purchases of diesel fuel for farm use is $120 million in fiscal 1988, $75 million in fiscal 1989, and $20 million per year thereafter. Extension of tax-free purchases to additional groups of exempt users will adversely affect compliance, and hence reduce the revenue gains that were anticipated in the 1987 Act. The Treasury Department estimates that amending the 1987 Act provisions to permit all groups purchasing for exempt uses to make tax-free purchases at the wholesale level, subject to such registration, bonding, and information reporting as the Secretary deems necessary, would result in revenue losses of at least $80 million per year on an ongoing basis (exclusive of losses attributable to nonrecurring timing differences). Thus, even if given the authority, the Treasury Department would proceed cautiously in extending the up-front exemptions and consider in each case what procedural safeguards would be appropriate to ensure compliance gains.

C. Refund and Credit Procedures

As an alternative to further revision of the collection procedures for the gasoline and diesel excise taxes, another possible approach to relieving the burden on exempt users would be to revise the current refund procedures. One possibility would be to provide an accelerated refund procedure for State and local governments or other exempt users. Under such a procedure, governments might be permitted to file for refunds weekly or monthly, rather than quarterly or annually. In addition to, or in lieu of, such a change, interest might be allowed on refunds. The Treasury Department would not recommend such changes. Although clearly preferable to current procedures from the standpoint of exempt users, these changes would not reduce their paperwork burden and would increase the burden on the Internal Revenue Service of processing refund claims.

A second possibility would be to amend the provisions of section 6416. One possible change would be to make section 6416 available for sales of diesel and aviation fuels. A second change would be to prohibit persons selling gasoline or diesel fuel to certain exempt users from including the tax in their prices. Under such a rule, the procedures of section 6416 would, in effect, be made mandatory. As part of this approach, section 6416 might be amended to provide for payment of refunds to the person selling gasoline or diesel fuel to certain exempt users, even if that person is not the taxpayer.

Expanding section 6416 and making it mandatory in certain situations could aid certain exempt users that purchase gasoline or diesel fuel at a point below that at which the tax is imposed. Such an approach, however, could also harm sellers by imposing a cash flow burden on them. As a result, it may harm, rather than help, some exempt users, especially smaller entities with little bargaining power. Some suppliers might simply refuse to sell to such entities rather than sell tax-free and wait for a refund; thus, such a change might affect the availability or the price (exclusive of the tax) of the fuel for such persons.

This concludes my prepared remarks. I would be pleased to respond to your questions.

FOOTNOTES

1/ A small percentage of this amount is transferred to the Aquatic Resources Trust Fund.

2/ Of these 12,000 persons, approximately 8,000 sold on a tax-paid basis and therefore remitted tax to the Federal Government.

3/ The estimated revenue increases for fiscal 1988 are larger than for the other years because movement of the collection point produces a one-time acceleration of tax collections. In the case of diesel fuel, an acceleration effect also exists in fiscal 1989, since in that year the Federal Government will receive tax on sales for a full year, but will pay refunds to farmers and other exempt users only with respect to sales during the period from April 1 through December 31, 1988.

4/ The Internal Revenue Service recently issued a notice (Notice 88-30) describing the procedures that will be applicable to tax-free purchases for the specified categories of uses. Under the notice, only purchases at the wholesale level will be permitted to be made tax-free. The notice also describes various certification, registration, and bonding requirements that must be satisfied by some or all of the persons that are permitted to make tax-free purchases.

5/ Purchasers for other exempt uses for which an up-front exemption has not been granted may face somewhat similar burdens.

6/ The rules discussed above that permitted State and local governments to make tax-free purchases of gasoline from wholesalers (under prior law), or under the section 6416 procedure, did not apply to farmers.

7/ S. 2067 would also permit farmers to purchase gasoline tax-free, even though such sales were not exempted from tax under pre-1988 law.

8/ These products increase the volume of gasoline used by the consumer but will escape taxation unless rules are implemented to tax them at or before the point at which they are added to gasoline. If Congress were to move the collection point further upstream to the refinery, procedures would have to be implemented to tax products added after removal from a refinery, but before removal from a terminal, in addition to products added after removal from a terminal.

DEPARTMENT OF THE TREASURY
WASHINGTON

March 17, 1988

Dear Senator Boren:

At the March 16 hearing before the Finance Subcommittee on Energy and Agricultural Taxation, I was asked to respond to the following questions regarding the administration of the excise taxes on gasoline and diesel fuel:

1. How does the Internal Revenue Service plan to increase its efforts to audit compliance with these excise taxes?

2. How many refund and credit claims for the diesel fuel excise tax does the Internal Revenue Service anticipate receiving and how much will it cost to process these claims?

3. How many refund claims by State and local governments and gasohol blenders for the gasoline excise tax does the Internal Revenue Service anticipate receiving and how much will it cost to process these claims?

4. How does the cost of processing refund and credit claims compare to the revenue gains attributable to the changes in collection of the gasoline and diesel excise taxes?

Allow me to respond to each of these questions separately.

1. Audit Efforts

Movement of the collection point upstream for both gasoline and diesel fuel taxes reduces the number of persons that are obligated to remit the tax. As a result of these lower numbers, the Internal Revenue Service anticipates auditing a much higher percentage of taxpayers and transactions. If the Service were to audit the same number of excise taxpayers under the new law as it did in fiscal year 1987, the percentage of taxpayers audited would increase dramatically. In the case of gasoline, for example, we expect that there will be only one-eighth as many taxpayers as under prior law, so that the percentage audited will increase by eight times, to over 50 percent. In addition, the Service is increasing the staff hours devoted to excise tax collection. Staffing applied to diesel fuel examinations, for example, increased 5 percent for fiscal 1987 over fiscal 1986.

The Service is also developing four new forms that will become attachments to Form 720, the excise tax return, beginning in the first quarter of 1989. These forms will increase the information collected on these excise taxes, including information on sales and inventories as well as on facilities and services. This information, in turn, will be used to develop statistical data for each category of excise tax in order to improve both the manner in which returns are selected for examination and the ability of the Service to match reported information with information from third parties.

2. Anticipated Refund Claims for the Diesel Fuel Excise Tax

The Service currently estimates that the number of total refund claims for the diesel fuel excise tax under the procedures adopted in the Omnibus Budget Reconciliation Act of 1987 will be approximately 1 million per year. The Service anticipates that the number of claims for credit of this tax will also be approximately 1 million.

There will be some small additional costs, such as transcribing an additional line on the income tax return, in processing credit claims, but these costs are minimal. Refund claims cost an estimated $4.20 per claim to process. There are also some additional costs for audit classification. Thus, the total cost of processing and classifying the anticipated 1 million diesel refund claims would be between $4.5 and $5 million. Based on current experience in processing excise tax refund claims, the Service estimates that the average time for processing these claims (including referral to the examinations division) will be 9 weeks.

3. Anticipated Refund Claims for the Gasoline Excise Tax

A. State and Local Governments

The Service estimates the number of governmental entities that could file gasoline excise tax refund claims to be 86,000. Many such entities will avail themselves of the section 6416 procedure to purchase tax-free and thus will not file refund claims. (Those persons selling to governmental entities under section 6416 are generally expected to take a credit rather than file for refund.) Other entities are expected to file only annually. If, however, every one of these governmental entities were to file a quarterly refund claim, the total number of claims would be less than 350,000 and the total annual processing cost for such claims less than $1.5 million.

B. Gasohol Blenders

Industry representatives estimate the number of gasohol blenders to be between 2,500 and 3,000. Using the higher number and assuming that every blender files weekly claims for refund, the annual number of claims would be 156,000 At a processing cost of $4.20 per claim, the annual costs for processing gasohol claims would be $650,000.

4. Revenue Estimates and Administrative Costs

Revenue estimates for various tax provisions generally do not take into account the processing costs of administering those provisions. This policy is based on the assumption that the Internal Revenue Service will find within its current budget the resources to administer the Federal tax law and will, if necessary, reallocate resources in order to do so.

The amendments to the Federal excise taxes on gasoline and diesel fuel, like other choices regarding tax provisions, offer both advantages and disadvantages. The collection procedures chosen for the gasoline and diesel taxes impose certain administrative costs, but they also offer administrative benefits. For example, they substantially reduce the number of persons remitting the tax and thus permit better and more efficient audit coverage. The administrative costs of these amendments are very small in comparison to the revenue gains they permit.

Sincerely

Dennis E. Ross
Deputy Assistant Secretary
(Tax Policy)

The Honorable David L. Boren
United States Senate
Washington, DC 20510

STATEMENT

OF

DANIEL B. SCHERDER

Mr. Chairman and Members of the Subcommittee:

I am Daniel B. Scherder, Vice President-Financial Administration of Peabody Holding Company, Chairman of the American Mining Congress Tax Committee, and a member of the National Coal Association Tax Committee. I am appearing before you today on behalf of the American Mining Congress (AMC) and the National Coal Association (NCA).

The American Mining Congress is an industry association that represents all segments of the mining industry. It is composed of (1) U.S. companies that produce most of the Nation's metals, coal, and industrial and agricultural minerals; (2) companies that manufacture mining and mineral processing machinery, equipment and supplies; and (3) engineering and consulting firms and financial institutions that serve the mining industry.

The National Coal Association is a trade association composed of over 200 members. The NCA directly or indirectly represents 90 percent of the coal producers of America. In addition to coal producing companies, NCA's membership also includes coal brokers, equipment suppliers, coal transporters, consultants, electric utilities and resource developers.

The American Mining Congress and National Coal Association appreciate this opportunity to present their views on the repeal of the up-front exemption from the federal diesel fuel excise tax for fuel purchased for off-highway use.

The stated purpose of the 1987 action was to prevent the evasion of the diesel fuel excise tax. In fact, insofar as users of diesel fuel for exempt purposes such as the mining industry are concerned, the repeal is nothing more than a forced loan to the government. Further, Congress provided that a forced loan is not to bear any interest.

Because the American mining industry is a substantial user of diesel fuel in its mining operations, this involuntary loan provision will have a particularly onerous impact on it. Diesel fuel is used to

power a multitude of different types of mining equipment, from trucks to drag lines to engines used to run standing machinery. These uses of diesel fuel are not highway uses and, accordingly, are not and have not been subject to the diesel fuel tax. Nevertheless, the provisions of the 1987 Act will require the mining industry to pay the federal diesel fuel tax on all the diesel fuel it purchases for these exempt purposes.

In order to get its money back from the government, the industry will have to then go through the additional, recordkeeping and administrative burdens associated with pursuing quarterly refund claims from the government. When the industry does get its money back, it will receive no interest from the government for the involuntary loan it has been forced to make to the government, regardless of how long it takes the Internal Revenue Service to make the refund.

The effect of this regime on the mining industry can be illustrated by its impact on the coal mining segment of the industry. The Pennsylvania Coal Association has estimated that approximately two to four gallons of fuel are used in the mining of one ton of coal. With respect to coal mined in that state alone, the Association estimates that the repeal of the off-highway-use up-front exemption will reduce the cash flow of the Pennsylvania coal mining industry by $6 million annually. For the entire U.S. coal mining industry, this would mean a cash flow reduction of approximately $100 million annually.

In other words, the coal mining segment of the industry could be forced to make a $100 million <u>interest-free</u> loan annually to the federal government. For the entire American mining industry, the involuntary, <u>interest-free</u> loan extracted under this regime could approach $250 million annually.

There are other additional costs that the repeal of the off-highway-use up-front exemption will impose on the domestic mining industry. The coal segment of the industry moves a substantial portion of its output, approximately 20 percent, by the inland waterway barge system. Since the repeal of the up-front exemption also will increase the costs of barge operators, the cost of this type

of transportation will rise. In addition, the State of Illinois has announced that the state sales tax must be paid on the refundable federal diesel fuel excise tax imposed on fuel purchased for off-highway use. This additional sales tax will impact the mining industry directly and indirectly.

Since the early 1980s, the U.S. mining industry has been in a depression. During this period the size of the industry has declined precipitously. The industry has been subjected to competition from producers that are wholly or partially owned, operated, or subsidized by foreign governments. In addition, the non-fuel mineral industry has had to deal with the reality that the higher grade, more-easily mineable reserves are now often located outside the United States. In the last one or two years, the domestic mining industry has finally begun to emerge from the depths of that depression. It has not, however, regained the strength that is necessary if the industry is to supply the raw materials upon which our industrialized economy depends. A reduction of the industry's cash flow resulting from the repeal of the off-highway use up-front exemption from the diesel fuel excise tax will be yet another complicating factor in the industry's efforts to regain its strength and its ability to supply the minerals needed for the nation's economy and its national defense.

In just the last five years, the federal income treatment in a number of areas for the mining industry has steadily declined. Mine exploration and development costs have been subjected to the corporate minimum tax. In addition, the current deductibility of these costs has been limited to 70 percent; the remaining 30 percent must be amortized over five years. Coal and iron ore percentage depletion has been reduced by 20 percent. Depletion, mine exploration costs and mine development costs have been subjected to recapture. Finally, general capital cost recovery incentives have been reduced by repeal of the investment tax credit and ACRS depreciation system.

To the extent that a problem of evasion of payment of motor fuel excise taxes does exist, it can be dealt with by a far more rational means then repeal of the off-highway use up-front exemption. For

example, there could be a precertification system under which legitimate users of diesel fuel for off-highway use, such as mining industry, could attest to their status as exempt users. There may well be other appropriate means of dealing with such tax payment evasion problems as do exist.

We applaud the efforts of Senator Warner and others who are pressing legislation to restore the very important, up-front exemption from the diesel fuel tax for the mining industry.

If corrective legislative cannot be enacted by the April 1 effective date of the repeal of the exemption, then legislation should be enacted simply postponing that effective date until appropriate corrective legislation can be devised and enacted.

The American Mining Congress and the National Coal Association appreciate the Subcommittee's concern with this issue and its willingness to examine it. We sincerely hope the Subcommittee and the Congress act promptly to correct this portion of the 1987 Act. Thank you again for this opportunity to present our views to the Subcommittee.

Statement of
Don Schieber, President
Oklahoma Wheat Growers Association
Before the
Senate Subcommittee on Energy and Agricultural Taxation
on
Payment of the Diesel Fuel Tax
March 16, 1988

Mr. Chairman and Members of the Subcommittee:

My name is Don Schieber and I am a wheat farmer from Ponca City, Oklahoma. I am here today representing the views of both the Oklahoma Wheat Growers Association, and the National Association of Wheat Growers. Accompanying me is Jack Kelsey, vice-president of the National Farmers Union and president of the Oklahoma Farmers Union. Jack is also a wheat farmer from Waynoka, Oklahoma.

The budget reconciliation act passed last December included a variety of revenue raising measures for the U.S. government. Among them was a new requirement to collect the 15-cents-per-gallon diesel fuel tax from farmers and others, such as custom harvesters, who are exempt from the tax because they use the fuel for off-highway purposes. The tax will now be collected at the wholesale level, rather than the retail level, which forces farmers to pay the tax up front, and then file for a refund at the end of the year.

It seems to me and all the other farmers across the country who use substantial amounts of diesel fuel to operate their farm machinery that this new way of collecting the tax will simply provide an interest-free loan to the U.S. government over a period of several months. Farmers, on the other hand, will have to add the anticipated tax outlays to their operating costs, which in most cases have to be financed. It's one thing to raise taxes as a way of reducing the federal deficit, but it's quite another to collect a tax that is not owed in the first place as an artificial way to bring in short term revenues.

The refund system provided for in the law does allow the farmer to ultimately recover his outlay, but only as the result of additional recordkeeping and paperwork. Also, quarterly refunds will not be possible for a great many farmers to request because of the requirement that a minimum tax of $1,000 be paid in that quarter before a refund can be equested. Even if the farmer qualified in one quarter, he would not necessarily qualify during other quarters of the year because of the seasonal patterns of diesel fuel use. So, most farmers will have to wait until the end of the year before filing for their refunds.

Agriculture is still struggling to recover from several of the worst years we've seen since the Depression. But at the same time, we've been doing our share to close the budget deficit that threatens the stability of the national economy. Commodity spending will decline by over 20 percent this year, compared to last year, because of structural changes brought about by the 1985 farm bill, which included a phase-down of income supports through 1990. The 1987 reconciliation bill further cut farm income by lowering target prices for both the 1988 and 1989 grain crops by 1.4 percent. So, the additional burden of paying taxes we don't owe is most unwelcome in the farm community.

Mr. Chairman, the wheat growers support legislation to permit farmers to continue purchasing diesel fuel tax-free for off-highway use. We are hopeful that the legislation can be enacted as soon as possible, since the new collection rule goes into effect April 1. The only recourse farmers presently have is to stockpile disel fuel supplies between now and April 1. This, of course is no solution to the problem. We therefore ask for your help in expediting the legislation, and also in requesting delayed implementation of the rule to allow time for the corrective legislation to be put into place.

Thank you very much for your consideration of this statement.

STATEMENT OF THE AMERICAN FARM BUREAU FEDERATION TO
THE SENATE FINANCE COMMITTEE, SUBCOMMITTEE ON ENERGY
AND AGRICULTURAL TAXATION
REGARDING THE COLLECTION OF DIESEL FUEL EXCISE TAXES

March 18, 1988

Presented by S.M. True, Jr., President, Texas Farm Bureau, and Member of the Board of Directors, American Farm Bureau Federation

Thank you, Mr. Chairman and members of the Subcommittee. My name is S.M. True. I am a farmer and rancher from Plainview, Texas. I operate a medium sized, cotton, wheat, feedgrains and cattle operation. I am President of the Texas Farm Bureau and am representing the American Farm Bureau Federation, the nation's largest organization of farmers and ranchers.

I am here today to share with you Farm Bureau's concern over an obscure provision of the Omnibus Budget Reconciliation Act of 1987 which will have a profound impact on millions of farmers and ranchers. This provision changes the collection point for diesel fuel tax from the retail level to the wholesale level. Beginning April 1 of this year, farmers will be forced to pay a 15-cent per gallon excise tax on diesel fuel and then file for a refund or credit. Farmers now have an excise tax exemption for off-highway uses of diesel fuel.

Today we are asking your favorable consideration of legislation that will permit farmers and ranchers to continue to buy fuel tax-free if it is used for off-highway purposes. If this provision is not changed, farmers and ranchers will be burdened with an additional operating expense which will total hundreds of millions of dollars in diesel fuel excise taxes. Although farmers will be able to apply for refunds of these taxes, cash flow problems and higher interest costs to agricultural producers will undoubtedly result.

Costs to agriculture would be substantial. According to the 1982 Census of Agriculture, annual farm diesel fuel use is approximately 3 billion gallons. At 15 cents per gallon, agricultural producers would be forced to pay approximately $400 million in diesel taxes. In my home state of Texas, the impact to agriculture would be about $30 million. On my farm, which is a fairly typical operation, my off-road diesel fuel consumption per year is approximately 8,346 gallons. This means that I will be forced to pay $1,251.90 in taxes to the Federal Highway Trust Fund for fuel used off the highway, on my farm in the production of crops and livestock. Included in my statement for the record are state farm diesel fuel use figures from the 1982 Census of Agriculture. These statistics dramatize the impact of this new tax on farmers nationwide.

This is a tax that farmers do not owe and should not have to pay. It means that I must borrow additional operating capital and that I will have higher interest costs. It means additional regulation and paperwork to obtain a refund. Timing couldn't be worse. This new expense and regulatory burden will be imposed when farmers must cut expenses and increase efficiency to survive.

Although many of the details of the refund system to be imposed are not yet clear, there may be some major inequities. The Internal Revenue Service has informed us that farmers may file for quarterly refunds if the refund for the quarter is $1,000 or more. This would require diesel fuel use of at least 6,667 gallons per quarter or 26,667 gallons per year. Only the very largest farmers use this much diesel fuel. In checking with USDA's Office of Energy, we have estimated that less than 20,000 farmers would qualify to file quarterly for refunds. Most would have to wait until the end of the tax year to file for a tax credit on IRS Form 1040.

To make matters worse, no interest would be paid by the I.R.S. for payments held prior to refund. In effect, farmers will be making interest free loans to the federal government. We think this is ridiculous. Ironically, the costs to the I.R.S. of distributing and

maintaining a refund system may outweigh the benefits of any revenue which may find its way to the Treasury.

Last, we would like to bring to your attention a problem which underscores the need for quick legislative action to restore the previous tax-free purchase method of diesel fuel for off-highway use. An excise tax for off-road diesel fuel could increase fuel costs and disrupt the distribution system. This could occur when farmers and other off-road users "top off" their storage tanks before April 1 to avoid paying the extra 15 cents per gallon. This could create sudden, artificial demand for billions of gallons of diesel fuel which could not be supplied by the current refining and distribution system. This problem could be especially serious since it would take place in the early spring, the peak fuel use period for spring planting. Additional strong demand will also exist during the same period for home heating oil, which is essentially the same product as diesel fuel. Higher diesel fuel prices and regional shortages could result.

Mr. Chairman and members of the Subcommittee, the new requirement for collection of farm diesel fuel taxes is unfair, it is of questionable benefit to the federal government, and it will create a new financial and regulatory burden on farmers and ranchers. It will increase production costs and may cause serious disruptions in fuel supplies which are essential in the production of agricultural commodities.

These concerns are shared by fifteen other major organizations which have cosigned a letter to all members of the House and Senate expressing the need for immediate action. I have included that letter for the record as part of my statement.

Three bills which would accomplish our objective have been introduced. Although the language of these bills is different to some extent, it is our understanding that each would restore the tax-free purchase of diesel fuel used off the road in the production of agricultural commodities. These bills include S. 2003 introduced by Senator Phil Gramm, S. 2067 introduced by Senator Kent Conrad, and S. 2075 introduced by Senator Thomas Daschle. Cosponsors of these bills now total more than 50. In the House, more than a dozen bills have been introduced, and cosponsors total more than 200. We commend these Senators for their leadership in dealing with this important problem and urge your swift, favorable consideration of these bills. The April 1 implementation date is quickly approaching.

Thank you.

88-190 - 88 - 6

FARM DIESEL FUEL USE AND POTENTIAL
EXCISE TAX EXPENSES TO FARMERS

STATES	FARM DIESEL FUEL USE 1982 (MILLIONS OF GALLONS)*	EXCISE TAXES @ $.15 PER GALLON (MILLIONS OF DOLLARS)	STATES	FARM DIESEL FUEL USE 1982 (MILLIONS OF GALLONS)*	EXCISE TAXES @ $.15 PER GALLON (MILLIONS OF DOLLARS)
U.S.	2,838	426	Montana	49	7
Alabama	34	5	Nebraska	150	22
Alaska	**	**	Nevada	5	.7
Arizona	22	3	New Hampshire	9	.1
Arkansas	83	12	New Jersey	6	1
California	167	25	New Mexico	13	2
Colorado	45	7	New York	44	7
Connecticut	3	.4	North Carolina	62	9
Delaware	5	.7	North Dakota	109	16
Florida	56	8	Ohio	83	12
Georgia	62	9	Oklahoma	68	10
Hawaii	8	1	Oregon	30	4
Idaho	45	7	Pennsylvania	38	6
Illinois	186	28	Rhode Island	**	**
Indiana	97	15	South Carolina	27	4
Iowa	184	28	South Dakota	80	12
Kansas	141	21	Tennessee	42	6
Kentucky	46	7	Texas	210	31
Louisiana	61	9	Utah	11	2
Maine	5	.7	Vermont	5	1
Maryland	14	2	Virginia	28	4
Massachusetts	2	.3	Washington	49	7
Michigan	64	10	West Virginia	4	.5
Minnesota	143	21	Wisconsin	81	12
Mississippi	67	10	Wyoming	11	2
Missouri	92	14			

*Source: 1982 Census of Agriculture, U.S. Summary, AC82-1-51, 1984.

**Less than 1 million gallons.

AMERICAN FARM BUREAU FEDERATION
225 Touhy Avenue • Park Ridge • Illinois • 60068 • (312) 399-5700
600 Maryland Avenue, S.W. • Suite 800 • Washington, D.C. • 20024 • (202) 484-2555

United States Senate
WASHINGTON, D.C. 20510

MARCH 16, 1988

STATEMENT OF THE HONORABLE JOHN WARNER
BEFORE THE SUBCOMMITTEE ON AGRICULTURAL AND ENERGY TAXATION,
COMMITTEE ON FINANCE
IN SUPPORT OF CHANGES TO THE PROCEDURE
FOR THE COLLECTION OF THE
DIESEL FUEL EXCISE TAX

Mr. Chairman, Members of the Committee, I am pleased to support your Subcommittee's efforts to find some suitable and enforceable way to collect the diesel fuel excise tax, without placing the burden of that collection on all off-road users of diesel fuel.

The recently-enacted Budget Reconciliation Act contained a revenue provision that would change the collection point for the diesel fuel excise tax on federal highway users from retailers to wholesalers. Clearly, this new tax collection procedure, which is scheduled to take effect April 1, was intended to strengthen enforcement and collection of the diesel tax from those who use our Nation's highways. I am sure we all agree that this is a worthy goal.

However, the unintended effect of this provision will be to force virtually all diesel consumers to pay the tax up front on their fuel. Only thereafter can those who can demonstrate that they did not use the fuel on a federally-funded highway be eligible to apply for a refund from the Internal Revenue Service.

Before this Act passed, a retailer, who was collecting the tax, was presumed to be able to distinguish between sales of fuel to highway and non-highway users. Under the new procedure a diesel wholesaler will have no idea who the end-user of the fuel will be and will thus have to charge the tax on all fuel sales.

The Reconciliation Act does provide for several exceptions: commercial aviation, home heating oil, state and local governments, and railroads. These exceptions are provided because it was generally believed that those categories of users could be easily identified as non-highway users at the wholesale level, and therefore not be required to go through the cumbersome procedure of applying for a tax refund or credit on a tax no one ever intended them to pay.

As you will no doubt hear, this provision, which once appeared so innocuous, will have a tremendous financial impact on off-road users of diesel fuel. While I know there has been a great deal of discussion of the impact this provision will have on farmers and state and local governments, I wanted to share with the Subcommittee its impact on two other industries that are heavily reliant on diesel fuel: fisheries and mining.

FISHERIES

This provision, which will effectively raise diesel fuel costs by 20%, imposes a severe cash drain on fishery vessel operators. These small businessmen operate on a narrow margin. They cannot afford to give the federal government thousands of dollars that they need to make mortgage and insurance payments on vessels, meet payrolls for crew members, and repair boats and replace gear. In fact, in many fisheries, fuel cost is the most significant cost associated with vessel operations. Fuel purchases account for over 27 percent of operating costs for vessel operators in the southeastern United States.

Further, this change in tax collection procedures will impose an onerous recordkeeping burden on these small businessmen least able to comply with it. Fishery vessel operators and owners will

have to maintain dependable and meticulous records of all fuel purchases for IRS inspection in order to obtain refunds of a tax they were never meant to pay.

Can you imagine having to keep meticulous records of every gasoline purchase you make for your car to get a refund on a tax you were never meant to pay? You would have to submit detailed versions of those records to the IRS annually and keep them for seven years in the event of an audit. All to get back money which was rightfully yours in the first place.

Relieving this burden is the goal of S. 2128, legislation which I have introduced with Senators Trible, Murkowski, Stevens, Mitchell, Cohen, Chafee, Pell, Sanford and Shelby.

MINING INDUSTRY

The same holds true for the mining industry. My second bill, S. 2166, would simply add them to the list of exceptions already enacted into law. I have made provisions in this bill to apply the same rules and regulations that will face diesel wholesalers to ensure that the tax is collected from those who are meant to pay it.

One example, pertinent to my state, is the effect this new procedure will have on the coal industry. The coal mining industry utilizes enormous quantities of diesel fuel in off-road vehicles and other machinery incident to mining and ore preparation at the mine site. These categories of uses, which have been historically exempt from the tax, would remain exempt. However, coal mine operators and other mining operators will be required to pay the federal excise tax and to seek recoupment through a refund or a tax credit. Our estimate is that this new procedure will result in the coal industry alone being required to "loan" up to one hundred million dollars to the federal government interest-free pending the IRS refund or tax credit.

Using accepted carrying charges on the lost use of that money it is estimated that this collection procedure will result in the coal mining industry losing six to ten million dollars annually at existing levels of use for diesel fuel. Additionally, the increased paperwork associated with filing for and pursuing refunds or utilizing the crediting procedures which the IRS has been directed to promulgate under the change of law will result in additional administrative costs to the mining industry.

This seems particularly ill-timed as the coal industry and other mining industries work to regain their world competitive position following the fall of the dollar. As they rebuild their domestic and international market, the last thing they need is to fill out even more tax forms and see this money removed from their crucially important cash flow.

I appreciate the improved tax enforcement intentions behind the original legislation contained in last year's Reconciliation Act, to eliminate documented and well-known abuses. However, the application of this new tax collection procedure across-the-board to all users of diesel fuel, no matter how unrelated their activities are to use of the Nation's highways, is a prime case of an over reaction to correct a specific problem.

I hope your Committee will be able to finalize work and report to the full Senate comprehensive legislation that will correct this situation. As we approach the April 1 effective date, with very little of the collection and refund machinery in place at the Treasury Department, I would hope that we in Congress can act in time to avoid the whole mess.

I compliment the Finance Committee for such a timely response to a very evident and immediate need.

Malcolm Wallop

STATEMENT OF SENATOR MALCOLM WALLOP--DIESEL EXCISE TAX HEARING--3/16/88

MR. CHAIRMAN, THIS IS NOT JUST A HEARING ABOUT THE COLLECTION ASPECTS OF THE DIESEL FUEL EXCISE TAX. IT IS MUCH MORE THAN THAT. BEHIND THE LEGISLATIVE RHETORIC AND BOOKKEEPING JARGON IS A SINGLE, STRAIGHT-FORWARD QUESTION THAT MUST BE ANSWERED. THE QUESTION IS SIMPLY: HOW CAN THE FEDERAL GOVERNMENT, NOW OR IN THE FUTURE, MORALLY OR ETHICALLY JUSTIFY COLLECTING A TAX FROM A PERSON WHICH IT KNOWS FULL WELL DOES NOT OWE THE TAX?

EVEN IF, OR WHEN, A RANCHER GETS THE EXCISE TAX REFUNDED, THE GOVERNMENT ISN'T GOING TO PAY ONE THIN DIME IN INTEREST OR A SINGLE DOLLAR FOR ALL THE ADDITIONAL BOOKKEEPING. THE AMERICAN FARM BUREAU FEDERATION INFORMED ME THAT THE WYOMING AGRICULTURE COMMUNITY USES MORE THAN 11 MILLION GALLONS OF DIESEL EACH YEAR. THIS MEANS THAT $1,650,000 IN TAXES ARE STILL GOING TO BE COLLECTED FROM FARMERS AND RANCHERS, ALTHOUGH THEY ARE NOT LEGALLY OWED. WHO HERE TODAY CAN TELL ME THIS WON'T HAVE A SERIOUS IMPACT ON THE CASH FLOW OF THESE PEOPLE?

ON A NATIONAL BASIS, AMERICAN FARMERS USE 2.8 BILLION GALLONS OF DIESEL FUEL EACH YEAR WHICH TRANSLATES INTO $426 MILLION...THAT WILL BE SURRENDERED TO THE IRS UNTIL A REFUND IS ISSUED. LOST INTEREST FROM SUCH AN AMOUNT MEANS TENS OF MILLIONS OF DOLLARS.

MR. CHAIRMAN, THE WYOMING AGRICULTURE COMMUNITY IS JUST BEGINNING TO SEE A LITTLE SUNSHINE AFTER A LONG STRETCH OF TOUGH TIMES. ANYONE WILLING TO JEOPARDIZE THE THIN PROFIT MARGIN THAT SOME OF THESE FOLKS OPERATE ON ONLY SHOWS A COMPLETE DISREGARD OF THEIR CIRCUMSTANCES. WYOMING RANCHERS AND FARMERS DESERVE CONGRESS' RESPECT, NOT CONTEMPT.

THE COLLECTION POINT CHANGE WILL HAVE A BROAD NEGATIVE IMPACT ON OTHER AREAS OF WYOMING'S ECONOMY. WYOMING HAS A LARGE NUMBER OF OTHER HIGH VOLUME TAX EXEMPT USERS -- DRILLING AND WELL SERVICE CONTRACTORS, MINES, AND CONSTRUCTION CONTRACTORS. THE CHANGE IN COLLECTION POINT WILL ADD AS MUCH AS 27% TO THE UP-FRONT COST OF FUEL FOR THESE USERS AND THE DRAIN ON THEIR CASH FLOW WILL BE SIGNIFICANT.

WYOMING DRILLING CONTRACTORS USED AN ESTIMATED 8.6 MILLION GALLONS OF DIESEL FUEL IN TAX EXEMPT USE DURING 1987. UNDER THE NEW LAW, THE CONTRACTORS WILL BE FORCED TO PAY $1.3 MILLION IN TAXES THEY DO NOT OWE AND AT A TIME WHEN THEY ARE IN FINANCIAL DIFFICULTY. THIS ADDED DRAIN ON CASH FLOW AND THE OUT OF POCKET COST OF COMPILANCE AND RECORD KEEPING REQUIREMENTS ON ALREADY STRAINED BUSINESSES COULD FORCE SOME OF THEM OVER THE EDGE INTO BANKRUPTCY OR AT LEAST FORCE THEM TO MAKE CUT BACKS IN OTHER AREAS, SUCH AS EMPLOYMENT.

THE DIESEL REFUND MECHANISM DOES NOT ADEQUATELY ADDRESS THE TAX EXEMPT USE PROBLEM. MANY FARMERS AND RANCHERS MAY NOT HAVE $1,000 OR MORE IN DIESEL TAX PER QUARTER IN ORDER TO USE THE QUARTERLY REFUND MECHANISM. ALSO, SINCE THEY ARE NOT GENERALLY REQUIRED TO MAKE ESTIMATED TAX PAYMENTS, THEY MUST WAIT UNTIL THEY FILE THEIR ANNUAL TAX RETURN TO RECEIVE THEIR REFUND.

EVEN THOSE TAXPAYERS ALLOWED TO FILE ON A QUARTERLY BAISIS, THERE IS NO GUARANTEE THAT TREASURY WILL BE ABLE TO PROCESS REFUNDS IN A TIMELY MANNER GIVEN THE HUGE INFLUX OF REFUNDS EXPECTED.

REGARDLESS OF WHEN THE REFUND IS FILED, THE FACT REMAINS THAT UNTIL IT IS RECEIVED, TAX EXEMPT USERS HAVE GRANTED UNCLE SAM AN INTEREST FREE LOAN. THE SAD AND UNFORTUNATE IRONY OF THIS IS THAT MANY OF THEM PROBABLY HAD TO BORROW THE MONEY TO PURCHASE THE FUEL TO BEGIN WITH.

THE CHANGE TO THE GASOLINE TAX COLLECTION POINT HAS BROUGHT ABOUT PROBLEMS OF ITS OWN. MANY WYOMING TOWNS AND MUNICIPALITIES ARE STRUGGLING TO PROVIDE ADEQUATE PUBLIC SERVICES IN THE FACE OF DECLINING TAX REVENUE. THE INCREASE IN THE UP-FRONT COST OF FUEL COMES AT A TIME WHEN THEY ARE LEAST ABLE TO HANDLE THE INCREASE. THE ADDITIONAL RECORD KEEPING REQUIRED TO ACCUMULATE THE DATA AND FILE FOR THE REFUND ADDS TO THEIR BURDEN.

I AM ALSO CONCERNED ABOUT THE POSSIBLE SHIFT IN THE COMPETITIVE RELATIONSHIP BETWEEN REFINERS AND INDEPENDENT MARKETERS. THE LOSS OF THE TAX DEPOSIT FLOAT MAY GIVE REFINERS THAT DISTRIBUTE TO BOTH RETAILERS AND WHOLSALERS A COMPETITIVE EDGE OVER INDEPENDENT MARKETERS. I HOPE THAT TESTIMONY FROM THE PETROLEUM MARKETERS WILL CAST SOME LIGHT ON THIS ISSUE AND WE WILL BE ABLE TO ADDRESS THIS ISSUE AT SOME POINT IN TIME.

MR. CHAIRMAN, I HARBOR NO DOUBTS THAT WE WILL WILL BE ABLE TO FIND A WAY TO DEVELOPMENT AN ALTERNATIVE APPROACH TO COLLECT DIESEL EXCISE TAXES -- ONE THAT DOES NOT PLACE UNNECESSARY BURDENS ON TAX EXEMPT USERS.

COMMUNICATIONS

STATEMENT OF NORMAN R. SHERLOCK

PRESIDENT AND CHIEF EXECUTIVE OFFICER

THE AMERICAN BUS ASSOCIATION

ON

COLLECTION OF FEDERAL FUEL TAXES

On behalf of the American Bus Association, I appreciate this opportunity to comment on the diesel fuel excise tax collection/exemption process. I commend the Committee for conducting this hearing. The American Bus Association represents more than 3,500 companies involved with bus regular route, tour and charter, airport and commuter services, and in businesses that are related to travel and tourism.

1. Collection Procedures for Diesel Fuel Excise Tax Modified by Omnibus Budget Reconciliation Act of 1987

As you know, the Omnibus Budget Reconciliation Act of 1987 changed the collection point of the diesel fuel excise tax. Previously, the tax could be collected on the sale by the retailer to the ultimate consumer of the fuel; the new law provides that the tax be collected at the wholesale level on the sale of fuel to any taxable fuel retailer. Collection of the excise tax on the sale of diesel fuel by wholesale dealers has has been made mandatory for all sales.

In addition, the new law repealed all exemptions for tax free sales and all provisions permitting exempt sales beyond

the wholesale level. However, in the Conference Report, the Treasury Department was given discretionary authority to exempt from the tax certain sales where the purchaser demonstrates that the fuel will be used in a non-taxable use and he registers and posts such bond as Treasury may require. Sales that may be exempted included:

(1) Diesel fuel sold for use as fuel in a diesel powered train,

(2) Aviation fuel sold for use as a fuel in an aircraft in commercial aviation,

(3) Taxable fuel sold for industrial use other than as a motor fuel, and

(4) Taxable fuel sold for the exclusive use of any state, a political subdivision of a state, or the District of Columbia.

All other exemptions from motor fuel excise taxes must be realized through the refund procedures following purchase of the fuels tax-paid.

2. <u>The Intercity Bus Industry and the Diesel Fuel Excise Tax Collection Process</u>

While ABA supports efforts to improve the efficient administration and collection of the diesel fuel excise tax, we maintain that the diesel fuel excise tax collection process has adversely affected the intercity bus industry.

Historically, Congress has encouraged the use of private intercity bus transportation. The Energy Tax Act of 1978, the

Highway Revenue Act of 1982, and the Tax Reform Act of 1984 all contained provisions exempting intercity buses from all or a part of the diesel fuel excise tax as well as other highway user taxes. This national policy stems from Congressional recognition that the intercity bus industry plays a unique and vital role in our nation's transportation system.

Under the law and regulations in existence prior to the 1987 Budget Reconciliation Act, bus owners and operators were given the option of paying the excise tax as the fuel was actually used in a bus on the highway. This option was available if the fuel was delivered into the bus operator's bulk storage tanks. However, the new law requires that the excise tax be collected earlier in the chain of distribution. Bus owners who utilize the procedure allowing them to pay the tax as the fuel was used must now pay the tax earlier, when the fuel is purchased. After paying the tax, the bus owner or operator applies for a refund (or credit) for 12 or 15 cents of the 15 cents per gallon tax. ABA members have been experiencing extensive delays, up to several years, in receiving refunds and, in addition, are burdened by the paperwork required to process the application. Further, the ABA members receive no interest on funds held by from the Internal Revenue Service.

We submit that increased savings and efficiency could be achieved by requiring bus owners and operators to initially pay only the 3 cents tax for which they are liable and not have the added burden of a claim for refund. In addition, such a move would eliminate the IRS' administrative burden of processing the claims for refund and the tax credit.

3. <u>Private Intercity Bus Industry is in Precarious Financial Condition</u>

Competition in the intercity bus industry has increased dramatically since the 1982 deregulation of the industry. For

the fiscal year which ended June 30, 1987, compared to the same periods ending June 30, 1986, operating revenues declined 12.1 percent, and revenue passengers carried decreased 19.1 percent. Net income declined from $26.7 million to $8.4 million. ABA believes that any additional burdens on the cash flow position of the intercity bus operator will narrow the already small margin of profit of many carriers forcing them to reduce service or cease operations.

As Congress has acknowledged in the past, the intercity bus industry provides affordable, convenient transportation to more than 350 million passengers annually. In comparison with other modes of transportation, intercity buses carry far greater numbers of senior citizens, students, military personnel, and women. An income profile of intercity bus passengers reveals that 58 percent have annual family incomes of less than $15,000.

Further, private bus companies receive no direct federal subsidy, yet most compete routinely with federally-subsidized entities such as Amtrak and the airlines. Amtrak is directly subsidized at a rate of approximately $35 per passenger. It is estimated that the current 12 cents per gallon diesel fuel excise tax exemption amounts to an indirect subsidy of only 8 cents per passenger for the intercity bus industry.

It should be noted that the 1987 Budget Reconciliation Act gave the Treasury discretionary authority to exempt certain sales from tax. One of these is the sale of fuel for use by a state, a political subdivision of a state, or the District of Columbia. ABA submits that exempting publicly owned buses while requiring the private bus operator to pay the tax up front would further harm the competitive position of the private intercity bus industry vis-a-vis public transit authorities. Public transit authorities are increasingly competing with private bus companies on commuter routes and in charters and tours. They enjoy tax exemptions due to their status as governmental entities and they

also receive federal subsidies. Publicly owned transit systems have received more than $1 billion annually from the Highway Trust Fund derived from taxes imposed on private highway users, including private intercity bus companies.

We understand that the Treasury Department is currently studying how to exercise its authority with respect to the diesel fuel excise tax and the possible exemption of state and local governments from the burden of having to pay the tax up front and then file for a refund. The American Bus Association urges that similar action should be taken with respect to the private intercity bus industry.

Conclusion

ABA submits that the current procedures requiring intercity bus companies to pay the diesel fuel excise tax up front and file for a refund or credit are discriminatory. The cash flow problem caused by these procedures seriously endangers America's vital bus transportation network. ABA urges the Subcommittee to recommend that the procedures for collection and payment of the excise tax be revised to reflect the true exemption of the intercity bus industry from a portion of the diesel fuel excise tax.

Alternatively, ABA requests that Congress require that the Treasury Department make refunds available to bus owners and operators within 60 days. If the refund is not made within that period of time, the Internal Revenue Service should pay interest on the refund to the bus owner or operator.

STATEMENT OF THE
AMERICAN PETROLEUM INSTITUTE

GASOLINE TAX

The original effort by Congress to change the point of collection of the gasoline tax was brought about because of concerns of massive tax evasion taking place in the gasoline marketplace. Estimates of loss of revenue to the Treasury ranged as high as $1 billion a year.

It was recognized, however, that moving the imposition of the tax further upstream could create major disruptions in the competitive structure of the petroleum industry. API worked closely with Congressional staffs and trade organizations, such as PMAA, SIGMA, and NPRA, to develop a proposal which would help eliminate evasion and stabilize competitive neutrality between majors, independents, wholesalers (jobbers) and dealers who market gasoline.

We recommended that the tax be imposed on the earlier of withdrawal into a truck from a refinery, pipeline terminal or marine terminal or on the first sale by a licensed taxpayer to an unlicensed purchaser. We further proposed that licensed taxpayers be limited to manufacturers, qualified wholesalers and qualified importers. In addition, we suggested that tax exempt purchases by anyone other than a licensed taxpayer be eliminated with any exempt consumers claiming refunds of any tax paid direct from Treasury.

It was recognized at the outset that the imposition of the tax at the terminal level could have a negative impact on the cash flow of certain intermediate dealers. However, there are too many variables such as the amount of time between removal from the terminal and ultimate consumer sale, the processing of sales, and terms of payment to precisely measure the cash-flow impact on any particular segment of the industry. API suggested as a partial remedy to the problem, that a transition period for payment of the taxes be established. Such a provision was never authorized. The Congress may want to consider alternative solutions.

The movement in the point of collection of tax to removal from a marketing terminal was eventually supported by all segments of the petroleum industry. API continues to believe that imposition of taxation when gasoline breaks bulk upon removal from a terminal is the appropriate way to carry out the original intent of Congress, i.e., to eliminate cheating by dishonest taxpayers permitted to purchase and sell gasoline free of tax downstream of the terminal level. The new law, among other things, has accomplished the following:

1. It addresses the issue of tax evasion. The new law has significantly reduced the number of taxpayers. Early estimates were that the number could go from around 8,500 to 600. Also, the elimination of most tax-exempt sales reduced the opportunities for tax cheating.

2. It maintains relative competitive neutrality since no marketer can move gasoline into the retail system (i.e., beyond the terminal rack) on a tax-free basis.

3. It enhanced compatibility with state motor fuel tax collection and enforcement and ongoing cooperative state/federal audit efforts.

4. No major costly accounting system changes were required to implement the new changes. In addition, compliance under the new law should be easy to audit by the IRS in view of the reduced taxpayers and tax-free movements.

Many of the administrative difficulties about which the Committee has undoubtedly heard were created because the Internal Revenue Service delayed so long in publishing regulations. It took almost a full year after Congress passed the statute until IRS published the proposed regulations on November 18 of last year, giving taxpayers only six weeks until the statute would go into effect on January 1 of this year. These problems were compounded by the fact that the proposed regulations contained a number of provisions which were either unworkable or imposed unreasonably onerous burdens on the industry. And, adding further to taxpayer frustration, the hearing on the proposed regulations did not occur until 5 days after the law went into effect. Since the hearing, the IRS has published a series of interim notices which indicate they will correct most of the problems in the proposed regulations, but we still do not have final regulations.

None of this negates the fact that the underlying system of the statute - imposing the tax when the gasoline breaks bulk - is sound and workable. We do believe that most of the administrative problems have been solved. Taxpayers are adapting to the new system and we feel it is basically working.

There are a few problems that remain which Congress may want to address, but we want to stress that the whole system does not need revamping.

Certain Tax Exempt Sales or Uses, Section 6416, IRC

It appears that Congress originally intended to reduce gasoline tax evasion through establishing a procedure whereby tax was due on all removals or sales of gasoline into the wholesale and retail marketplace from customs custody, refineries and terminals, even on sales to entities which would not be subject to tax. The new procedure of levying the tax on the removal or sale and obtaining refunds or credits directly from the IRS for control purposes, was established by the original legislation.

Whether intentional or inadvertent, section 6416 IRC was not modified or repealed. This section allows the "taxpayer" (the registered importer, refiner or terminal operator) to grant its exempt customers a refund or credit for overpayment of taxes. It also allows taxpayers to grant refunds or credit to intermediate wholesalers (jobbers) and retail dealers, for overpayment of taxes where they purchase tax paid gasoline and subsequently sell it to exempt entities and for exempt uses. Appropriate proof of exempt use is required in either case.

Generally, section 6416 is being used by registered taxpayers to effect the refund process for taxes overpaid by exempt entities, or because of exempt uses. The problem lies in that section 6416 allows taxpayers to grant refunds or credits; it is not mandatory. Some taxpayers have chosen not to effect refunds or credits under section 6416. This has caused some difficulty for unregistered wholesalers (jobbers) and retailers served by these taxpayers. These unregistered middlemen must pay the tax to their supplier, but in some cases their exempt customers have refused to pay them the invoiced taxes. These middlemen, not being ultimate users or taxpayers, have no clear, documented procedure for obtaining timely refund of overpaid taxes. Most of the problems appear to be with taxed sales of gasoline to state and local governments through wholesalers (jobbers) and retailers. To solve this problem, the most apparent remedy is to make the use of section 6416 mandatory rather than discretionary for all gasoline taxpayers. This would ensure that all registered taxpayers provide the same opportunity to their customers and to ultimate consumers who have claims for refund or credit of overpaid taxes.

As an alternative, repealing section 6416 would also eliminate the problem of disparity between taxpayers granting and not granting refunds or credits. This would require all consumers to make their claims directly to the IRS; but, it would not solve the problem of state and local governments and other exempt users

having their limited funds tied up for what appears to be an undesirable length of time.

Section 4221, IRC

If Congress intends for those entities identified in Section 6416 to purchase gasoline tax free, it will require a conforming technical amendment to reinstate the application of Section 4221 to the gasoline tax. If this is not done, industry is concerned that the IRS will take the position that Section 6416 application is limited to situations where the tax has been paid. Under that analysis, a direct sale by a taxpayer to a person identified in Section 6416 would be outside the scope of Section 6416 because those sales were originally covered by Section 4221 which has been eliminated. For example, where taxpayer A sells to B (wholesaler) who sells to C (State or local Government), this situation is covered by Section 6416. If, however, taxpayer A sells directly to C (State or Local Government), Section 6416 would not be applicable until taxpayer A paid the tax. It is inconsistent to retain Section 6416 without the companion Section 4221. Our recommendation is that if Congress intends for Section 6416 to remain applicable, it should reinstate Section 4221's applicability to the gasoline tax.

Gasoline Blend Stocks and Additives

Another issue with which the industry is concerned is the treatment of blend stocks and additives under the gasoline tax.

Paragraph 48.4081-1(e)(5) of the proposed regulations restates the definition of the term 'gasoline blend stocks' set out in the statute..."any petroleum product component of gasoline," I.R.C. Section 4082(a). The proposed regulations then add modifying language "that can be blended for use in a motor fuel." The definition then lists only three components as examples of gasoline blend stocks. The proposed rules treat the definition of "products commonly used as additives..." similarly. These definitions are too broad and general to allow designated taxpayers, purchasers and the IRS to know with any reasonable degree of certainty which gasoline components are to be considered subject to tax.

The purpose of including blend stocks and additives in the definition of gasoline is to prevent evasion of the gasoline tax that could occur if components were purchased tax-free and blended to produce gasoline, and no taxes were paid on the sale of the gasoline. To eliminate the ambiguity created, we believe a list that specifies which products are to be considered "gasoline blend stocks" and "additives" for gasoline tax purposes is a necessity.

The IRS in its Advance Notice 88-16 relating to the gasoline excise tax recognized that the definition of the terms "blend stocks" and "additives" contained in the proposed regulations do not permit taxpayers to determine with certainty whether certain products would come within this definition. Thus, the Service expressed its intent to list, by Revenue Ruling or other administrative pronouncements, specific products that will and specific products that will not be considered to be blend stocks or additives.

The petroleum and petrochemical industry is awaiting IRS guidance in this area. However, should the IRS fail to remove the ambiguity created, it may be necessary to seek a legislative technical correction to resolve this issue.

Tax on Gasohol

As contained in the proposed regulations published in the Federal Register on November 18, 1987, a registered gasohol blender could pay 3-1/3 cents reduced rate of tax on purchases of gasoline for blending with alcohol to produce gasohol. However, to qualify for the reduced rate of tax, the gasohol blender was required to purchase both the gasoline and the alcohol that are blended together to produce gasohol from the same terminal. To address

concerns expressed by gasohol blenders, the IRS issued Notice 88-2 which provided a transitional rule that under certain conditions will allow all registered gasohol blenders to purchase gasoline at the reduced rate of tax. In general, the requirements contained in the proposed regulations were delayed until April 1, 1988, and for the interim period, the registered gasohol blender could purchase the gasoline for gasohol blending at the reduced rate from a location other than where the alcohol is purchased. A second interim notice, 88-34, extended the transitional rule through June 30, 1988.

API would like to suggest an alternative procedure which would require the full payment of the tax on the purchase of gasoline but would provide a procedure whereby a gasohol blender could obtain timely credits for tax paid on fuel used to blend into gasohol. If gasohol is sold, the 3.1 cents per gallon rate would be imposed. If gasoline is sold by a registered producer to a registered gasohol blender, the tax of 9.1 cents per gallon rate would be imposed; however, the gasohol blender could claim a credit for the difference of the tax between gasoline and gasohol from the registered producer by providing forms, prescribed by Treasury, certifying the volumes of fuel used to produce gasohol.

DIESEL TAX

With respect to the change in incidence of the tax on diesel fuel (I.R.C. Sec. 4091), API sees some of the same problems encountered in connection with gasoline tax collection and we understand the concerns of consumers such as farmers, marine operators, construction contractors, drilling contractors, mining operators, exporters, timber companies and many other off-highway diesel users. The elimination of tax free sales places a significant burden on them by requiring them to seek refunds of tax paid on diesel fuel used for non-taxable purposes. The rationale for the change last year, according to the Finance Committee report, was similar to that for gasoline; i.e. to reduce opportunities for evading payment of the taxes. Congress believed that collection of the tax at a point in the distribution system with a smaller number of taxpayers provides for more efficient administration of the tax since there are fewer taxpayers for the IRS to monitor. The bill, however, went a step beyond just moving the tax up the distribution chain by providing that tax-free sales for certain exempt uses are repealed. The statute as finally enacted did provide that the Secretary might exempt railroads, airlines and state and local governments. There is a fourth category of exemption specified which may have been intended to cover farm and other off-highway use but Treasury has not construed it in that manner. The provision, I.R.C. Section 4093(c)(3), states "the tax imposed ... shall not apply to taxable fuel sold for use by any purchaser other than as a motor fuel." In pre-regulation comments API suggested to Treasury that in interpreting "use... other than as a motor fuel" they refer to I.R.C. Section 6421 which defines off-highway business use. IRS, however, has stated they do not believe that was Congressional intent and, therefore, they do not have the statutory authority for that interpretation.

If the Congress decides to authorize tax-free sales of diesel to farmers and other off-highway users, it could define I.R.C. Sec. 4093(c)(3) "use other than as a motor fuel" by reference to I.R.C. Sec. 6421. Any tax free sales should be accompanied by some requirement of registration and certification in order to enable IRS to audit and enforce compliance.

STATEMENT OF AMERICAN PULPWOOD ASSOCIATION INC.
ON THE
IRS TAXATION OF OFF-ROAD DIESEL FUEL
TO THE
SENATE SUBCOMMITTEE ON ENERGY AND AGRICULTURAL TAXATION
COMMITTEE ON FINANCE
MARCH 16, 1988

The American Pulpwood Association appreciates the opportunity to provide oral and written comments on the issue of tax-free sales of diesel fuel for off-road use.

Before I start, let me mention that the American Pulpwood Association Inc. is a nationwide, non-profit trade association responsible for issues that surround the safe and efficient harvest and transportation of forest products from the woods to the mill. APA members include the small businessmen independent logging contractors who harvest and transport pulpwood and timber, firms which purchase pulpwood and manage forest lands, and equipment companies that manufacture pulpwood and timber harvesting and processing equipment.

Like our colleagues in the farm community, we ask you to support and cosponsor legislation that will permit independent logging contractors to continue to buy tax-free diesel fuel that is used for off-highway felling, skidding, and loading operations which are performed to move timber and pulpwood from the forest to a point where it can be put on a truck. Like many other off-highway fuel users, our members were caught by surprise by the provisions of the 1987 Budget Reconciliation Act, which changed the diesel fuel tax collection point from the retail to the wholesale level.

This off-road diesel fuel tax collection will have a significant undesirable impact on our nation's independent logging contractors. On a nationwide basis, these logging contractors use feller-bunchers, delimbers, forwarders, loaders, cable yarders, and a variety of other diesel-powered off-road equipment to harvest some 227 million cords (or cord equivalents) of pulpwood and saw timber each year. We know from past studies that it takes an average of two gallons of diesel fuel per cord to harvest these trees, move them to roadside, and load them on road trucks. This means that these contractors are using approximately 454 million gallons of off-road diesel fuel each year. If the IRS starts collecting a 15¢ per gallon tax on this off-road fuel on April 1, the nation's logging contractors will end up coughing up approximately $68 million each year and then having to file for a refund or tax credit to get their money back.

The impact of the collection of off-road diesel fuel taxes on individual logging contractors is significant. We gathered some data (see attached) that indicates that these small businessmen will have negative cash flow impacts of $1,000 to $33,000 due to the proposed collection of tax on off-road diesel fuel.

During my frequent visits to logging operations across the nation, I've noted that independent logging contractors are small businessmen who operate on very tight profit margins. They work hard to make ends meet, and they have the same type of cash flow problems that many small, independent businesses experience. Requiring these logging contractors to pay up-front tax money on off-road use of diesel fuel is unfair and will cause severe economic problems for some whose businesses already are in fragile financial condition. On behalf of these independent logging contractors, let me say that what IRS is proposing, collecting tax money and then refunding it to them sometime in the future, amounts to what we think is an interest-free loan and an unconscionable practice.

Although we are not fully up to speed on the proposed IRS refund system, we know that the many small logging contractors who use less than 7,000 gallons of off-road fuel quarterly will be hit the hardest. These off-road diesel tax dollars will probably take as long as 14 months to find their way back to independent logging contractor business accounts. We're also concerned that some independent logging contractor operations may not have taxable income in a given year against which an off-road diesel fuel tax credit could be applied. In this case, we assume the credit would be carried forward and, again, feel this is unfair because independent logging contractors may need this money to help with cash flow problems.

We're in complete support and will work for passage of the Combest bill (HR 3865) and the de la Garza bill (HR 3866), which both permit tax-free sales of diesel fuel used off-road. We'll also be working to encourage Congressman Daub, Congressman Smith, Congressman Jontz, and Senator Gramm to change the wording in their bills (which currently only cover farm operations) to include other aspects of agriculture and forestry including the planting, growing, cultivation, protection, and logging of timber and pulpwood.

We've not had the time or means to quantify the impact of this off-road diesel fuel tax collection on our members who own and manage forest land. We conservatively estimate mechanical site preparation, reforestation, road building, and forest management operations on their 69-million acres of industrial forest holdings use 100-million gallons of diesel fuel per year . . . which accounts for another $15 million cash flow impact on these companies. This does not include the off-road diesel fuel use on small forest holdings, which accounts for about 70% of the nation's commercial forest land.

To those IRS and other administration tax executives who are here, we respectfully ask for an agriculture and forestry "deferment" or "exemption" from this off-road diesel fuel tax collection at the wholesale level until we can achieve the passage of legislation which will permit tax-free sales of diesel fuel for off-road use.

We thank you for calling this hearing on an issue of great importance to our independent logging contractor members. We hope that you and your colleagues will be able to quickly pass some legislation which will correct the unfair taxation of off-road diesel fuel that is used in agriculture and forestry.

NATIONWIDE IMPACT OF EXCISE TAX COLLECTION ON OFF-ROAD DIESEL FUEL USED FOR TIMBER AND PULPWOOD HARVESTING

PULPWOOD HARVEST (1987)

	94	million cords annual consumption (1)
-	34	million cords sawmill residues
	60	million cords annual roundwood pulpwood harvested

SAW TIMBER HARVEST (1977)

65,176 million board feet (2) divided by 390 board feet/cord (3) = 167 million cords

OFF-ROAD DIESEL FUEL USED TO HARVEST PULPWOOD AND SAW TIMBER

Approximately 2.0 gallon/cord (4) used in average harvesting system to move pulpwood and timber from the stump to on board the haul truck.

	60	million cords pulpwood
+	167	million cords saw timber
	227	million cords total harvest

227 million cords x 2.0 gallon/cord = 454 million gallon off-road diesel fuel used.

454 million gallon x 15¢ tax collected/gallon = $68.1 million

$68 million dollars will be collected annually by IRS on off-road diesel fuel used in pulpwood and timber harvesting.

Richard Lewis
APA Vice President
3/2/88

Footnotes:

(1) "Monthly Pulpwood Summary," December 1987, American Pulpwood Association.

(2) "Forest Statistics of the U.S., 1977," USDA Forest Service.

(3) "Pulpwood Statistics," 1986, Wood Volume Conversion Factors, p. 70, American Pulpwood Association.

(4) "Fuel Survey," 1987, American Pulpwood Association.

EXAMPLES OF INDIVIDUAL LOGGING CONTRACTOR IMPACTS FROM EXCISE TAX COLLECTION ON OFF-ROAD DIESEL FUEL USED FOR TIMBER AND PULPWOOD HARVESTING

SMALL LOGGING CONTRACTORS

1) Bucky Williams, Wilcox, PA
   - Crew size: Two 2-man crews.
   - Equipment: Two skidders. One cable yarder
   - Off-road diesel fuel consumption: Approx. 7,000 gal./year
   - Cash flow impact: -$1,050.00

2) Ray Hunt, Omega, GA
   - Crew size: One crew.
   - Equipment: One feller-buncher. One grapple skidder. One loader.
   - Off-road diesel fuel consumption: 22,500 gal./year
   - Cash flow impact: -$3,375.00

3) H. C. Salter, Alexandria, LA
   - Crew size: One crew.
   - Equipment: Two skidders. One feller buncher. One loader.
   - Off-road diesel fuel consumption: 15,330 gal./year
   - Cash flow impact: -$3,300.00

Additional note: Mr. Salter states his diesel fuel supplier is preparing to collect 15¢/gallon excise tax retroactively back to April 1, 1987!

LARGE LOGGING CONTRACTORS

1) Earl St. John, Spalding, MI
   - Crew size: Seven crews averaging 5 men each.
   - Equipment: Mix of skidders, feller-bunchers, slashers, bulldozers, graders, delimbers, etc.
   - Off-road diesel fuel consumption: 218,000 gal./year
   - Cash flow impact: -$32,700.00

2) Bennett Timber Co., DeRidder, LA
   - Crew size: Twelve 2-man crews.
   - Equipment: One prehauler per crew (total 12)
   - Off-road diesel fuel consumption: 27,300 gal./year
   - Cash flow impact: -$4,095.00

3) Deck Trevitt Logging, Forsyth, GA
   - Crew size: Two 5-man crews
   - Equipment: Two feller-bunchers. Three grapple skidders. Two hydraulic loaders. One crawler tractor. One motor grader
   - Off-road diesel fuel consumption: 57,000 gal./year
   - Cash flow impact: -$8,550.00

4) Pine Timber Co., Oglethorpe, GA
   - Crew size: Two 6-man crews.
   - Equipment: Four grapple skidders. Two feller-bunchers. Four hydraulic loaders. Two crawler tractors. One motor grader.
   - Off-road fiesel fuel consumption: 72,800 gal./year
   - Cash flow impact: -$10,920.00

The American Waterways Operators

Executive Offices

1600 Wilson Boulevard
Suite 1000
Arlington, VA 22209

Tel. 703 841-9300

March 16, 1988

Honorable David L. Boren, Chairman
Subcommittee on Energy and
Agricultural Taxation
Committee on Finance
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

On behalf of The American Waterways Operators (AWO), the national trade association of the inland and coastal barge and towing industry, I wish to submit comments on the Omnibus Budget Reconciliation Act of 1987 which changes the point of collection for highway use diesel fuel taxes. This industry will be forced to pay hundreds of millions of dollars annually in taxes not owed as a result of this change, which will go into effect April 1, 1988.

AWO member companies operate towboats, tugboats and barges on the East, West and Gulf Coasts, and on the inland waterway system, using approximately 1.6 billion gallons of diesel fuel per year. Over one half of the onboard jobs in the U.S. Merchant Marine have been created by the towing industry. In a typical year, there are more than 125,000 moves to and from over 200 U.S. cities; 87 percent of all U.S. cities are served by tug-barge moves. Almost 60 percent of grain exported by the United States is moved to seaports in barges, and one of every five tons of coal produced in the nation is carried by barge. Barge transportation accounts for 40 percent of U.S. petroleum movements. Our vessels transport about fifteen percent of the nation's intercity freight for just two percent of the total freight bill. Mr. Chairman, I'm sure you can attest to the economic benefits that the availability of waterborne freight transportation moving through the Port of Catoosa has brought to the state of Oklahoma and the nation.

Fierce competition is the chief hallmark of the tug and barge industry which produces a bounty for American shippers and consumers: quality service, innovation and, most of all, low prices. Thus, margins tend to be razor thin in the best of times. The line between survival and bankruptcy is always very narrow for barging companies.

In other words, anything which affects the thin margin threatens the existence of domestic water carriers. And, the fifteen cent per gallon tax on diesel fuel for highway purposes, collected at the wholesale level, takes dead aim at the towing industry.

Clearly, Congress did not intend that commercial waterway operators be asked to pay a tax they are not statutorily liable for. Our industry was simply caught up inadvertently in the noble effort to streamline collection of the tax and barricade against cheaters. Congress signaled its actual intent, we believe, by exempting the rail and commercial aviation modes of transportation, overlooking in those exemptions the water transport industry.

Towing vessels are not fueled in a manner which facilitates diversion to highway use. Our industry purchases fuel from midstreamers or diesel

fuel suppliers who buy directly from refineries. The refineries fill fuel barges or fuel flats, typically with a 10,000 gallon capacity, with diesel. These fuel barges are used to pump diesel directly into the towboats and tugboats used to push or pull our freight-carrying barges. This procedure is done either in the channel or at the water's edge. On the East Coast, tugboat operators buy their fuel from marine docks located at oil refineries. There is no evidence of any attempts to divert waterway fuel for highway purposes.

We have heard that a period of twelve to eighteen months may elapse before initial refunds will be processed and rebated by the Treasury Department -- with the towing industry therefore floating a $240 to $360 million loan to the government!

This massive loan from the private sector, interest free, constitutes as much as 20 percent of the industry's aggregate average revenues. Further, many AWO member companies have advised that their quarterly excise tax payments now exceed their quarterly income tax payments -- in fact, many of these companies are operating at no profit whatsoever. This new highway tax requirement not only places a staggering cash flow burden on the barge and towing industry, but further places our members at a severe competitive disadvantage with the railroads which are not subject to this substantial cash flow shortfall because they were exempted under the Reconciliation Act.

As of April 1, inland waterway operators will be forced to begin paying the highway tax and will continue to pay the Inland Waterway User Tax. This waterway tax on diesel fuel has been in effect since 1980 and will gradually increase from the current rate of ten cents per gallon to twenty cents per gallon on January 1, 1995, according to the schedule you and your colleagues on the Finance Committee and House Ways and Means Committee developed as part of the Water Resources Development Act of 1986 (P.L. 99-662). The user tax increase adopted in P.L. 99-662 was far less than the level of waterway user taxes the Administration had been seeking since 1981 because Congress recognized the importance of a competitive transportation system and the need to allow inland waterway operators to recover from the economic depression of the early and mid-1980's. Now, on top of this waterway fuel tax, inland towing companies are being asked to pay an additional fifteen cents per gallon on diesel fuel. Approximately 550 million gallons of diesel fuel are used annually on the inland waterway system ... this will mean $82.5 million in new user taxes this segment of the industry will be forced to pay.

Mr. Chairman, as you well know, domestic water carriers and other off-highway users of diesel fuel must begin up-front payment of the highway diesel fuel tax sixteen days from today. We urge the Subcommittee and full Committee and members of the House Ways and Means Committee to act promptly to correct this inequity before the effective date of April 1. I assure you and your colleagues that the barge and towing industry will work with you and the Treasury Department and Internal Revenue Service on a precertification exemption system that would be imposed on all purchasers of diesel fuel to achieve the original intent of securing payment of the highway tax.

We appreciate the opportunity to submit our comments to you.

Sincerely,

Joseph Farrell

Statement

of

The Associated General Contractors of America

The Associated General Contractors of America represents more than 32,500 firms, including 8,400 of America's leading general contracting companies which are responsible for the employment of more than 4,000,000 individuals. These member contractors perform more than 80 percent of America's contract construction of commercial buildings, highways, industrial and municipal-utilities facilities.

The Associated General Contractors of America welcomes the opportunity to comment on the need to restore the up-front diesel fuels tax exemption for off-highway business use.

As an industry comprised primarily of small businesses, the repeal of the up-front diesel fuels tax exemption comes as a special hardship to construction. Construction is an energy intensive industry, consuming large quantities of diesel fuel in off-highway uses, such as earth moving for highway and dam projects and fueling asphalt hot-mix plants and paving machinery.

Since the diesel fuels tax is a user-fee, assessed on highway users to pay their share of the construction and rehabilitation costs of the nation's highway system, off-highway uses have rightfully been exempt from the tax in the past.

The repeal of the up-front exemption may at first seem like a small change in tax law; however, the change brings major cash management problems to the construction industry.

To give the Committee some insight into the problem from the construction industry's standpoint, AGC will highlight a number of aspects of this change that are particularly troubling to our industry:

First, it is important to consider the quantity of diesel fuel that even a typical small contractor uses in off-highway construction activities over the course of a year. AGC conducted a survey in December to determine the impact of the tax change. The survey indicated that small highway contractors, on the average, use 200,000 - 300,000 gallons of diesel fuel in off-highway activities each year; small to medium sized asphalt paving contractors use 600,000 - 700,000 gallons of diesel fuel annually; and one of AGC's larger contractors, who constructs major dams, uses up to 8 million gallons of diesel fuel in one year.

At 15.1 cents per gallon, the cash flow implications of this tax change are obviously very significant to these contractors. For that average highway contractor using 200,000 to 300,000 gallons of diesel fuel each year, the firm will carry an additional $30,000 - $45,000 annual cash flow burden; the asphalt paving contractor will carry an additional $90,000 - $105,000 cash flow burden, and the large contractor will carry an additional $1.2 million annual cash flow burden. For small, medium, and large contractors, these are all sizeable sums of cash that the contractors will now have to pay the government up-front.

Second, AGC understands that the Treasury is contemplating a quarterly refund process for refunds of $1,000 or greater, and

an annual process for other refunds. Anticipating that there will be a flood of refund applications, we expect that there will be a delay, and likely, a lengthy delay in processing refund checks -- All without interest for the government's use of our money.

Third, construction contracts are often long term in nature and fixed price. Since this tax change will significantly increase the price of fuels on existing contracts, the construction industry will have to absorb these increases within already agreed upon contract prices.

AGC recognizes and fully supports the desire of Congress to close loopholes in the tax system which permit the unscrupulous to evade payment of taxes they rightfully owe. AGC has a hard time understanding, however, the fairness of a tax provision which requires individuals to pay tax for a legitimate non-taxable activity and then apply for a refund which they hopefully will receive sometime in the future, without interest. Combined with all the other tax accounting changes that have taken place over the past two years which have adversely affected the construction industry, this latest change is most burdensome.

Since enactment of the exemption repeal provision in December of last year, construction, agriculture, and other industries have been seeking a remedy to the situation. In response, a number of bills have been introduced addressing different industries' concerns. In the House, a bill sponsored by Congressman Combest and 75 co-sponsors, restores the exemption for agriculture and most other off-highway uses. In terms of equity, this is the fairest approach.

As the Committee knows, four categories of diesel fuel users were specifically mentioned in the exemption repeal provision passed last December as deserving of consideration for continuation of the up-front exemption -- diesel trains, non-commercial aviation, non-motor industrial uses and state and local governments.

The Treasury is authorized to screen entities in these four categories, on a case-by-case basis, and convey tax exempt status to them provided they meet certain requirements documenting their non-taxable use. AGC understands that, provided the IRS has sufficient manpower to screen and audit entities which apply for the up-front exemption, the revenue impacts of this process should be negligible.

AGC believes that if this process is fair for these four categories of diesel fuel users, the process should be extended to other qualified off-highway business use. We fail to see the equity in limiting the opportunity to seek the exemption to some types of industries and users, while excluding others with an equal claim to the exemption.

As an industry, construction will stand toe to toe with agriculture, aviation and any other qualified off-highway users of diesel fuel. Upon examination, AGC believes the Committee will fail to distinguish any reasonable difference in the legitimacy of construction's non-taxable status compared with the other qualified off-highway uses.

In closing, AGC urges the Congress to quickly address the inequity of the repeal of the diesel fuel tax exemption for all industries which have legitimate non-taxable uses. The April 1 effective date is almost upon us.

Again, AGC most appreciates this Committee's desire to examine the issue and looks forward to working with the Committee as it examines options to address this problem.

Brown & Root, Inc. Post Office Box Three, Houston, Texas 77001
A Halliburton Company

Joe M. Stevens, Jr.
Vice President
Employee Relations & Corporate Affairs (713) 676-3305

March 7, 1988

Honorable David L. Boren
United States Senate
453 Russell Senate Office Building
Washington, D.C. 20510-3601

Dear Senator Boren:

We were pleased to learn that your Finance Subcommittee on Energy and Agricultural Taxation will hold a March 15th hearing on the collection of fuel taxes. In lieu of formal testimony, we are writing you to urge your assistance in restoration of the up-front tax exemption for off-highway diesel fuel purchases, and would deeply appreciate your including this letter in the hearing record.

The Budget Reconciliation Act of 1987 made several key changes to the Internal Revenue Code with respect to the diesel fuels excise tax, which were intended to prevent tax evasion schemes estimated to cost the Highway Trust Fund several hundred million dollars annually in lost revenues.

Included in the Act is a provision, to become effective April 1, 1988, that repealed the up-front exemption of federal excise taxes on diesel fuel purchased for off-highway use. The taxes will continue to be non-taxable; however, we will be required to pay the tax at time of purchase, and then apply to the Treasury Department for a refund which would likely be subject to lengthy delays.

This is a major impact on industries which consume large quantities of diesel motor fuels in off-highway uses. It creates a heavy cash flow burden and significant costs for interest expense and administrative requirements. For 1987, Brown & Root's off-highway diesel fuel consumption was 2.6M gallons of diesel fuel, of which, conservatively, 95% was for off-road use. Had the repeal been in effect in 1987, Brown & Root would have experienced an additional average monthly cash outflow of about $30,000 per month. The additional interest expense would be about $4,000 quarterly, based on current rates of interim financing.

Our parent company, Halliburton, would have had to pay $1,132,500 for its 1987 purchases of 7.5M gallons of off-highway diesel fuel, a monthly cash outflow of $94,375. Brown & Root's major uses for diesel fuel are for heavy equipment (large and small cranes, dirt moving equipment, paving equipment, etc.), marine vessels (barges, supply boats, etc.), diesel powered machinery of various utilities (e.g. welders, compressors, generators, pumps, etc.). Halliburton's major use is for equipment engines and down hole applications.

Please consider sponsoring or co-sponsoring legislation to restore the up-front exemption. With bi-partisan support, H.R. 3865, which restores the up-front exemption for construction and other industries, was introduced in the House. We urge your support of similar legislation in the Senate.

Our companies have suffered through a severe economic depression, and continue to struggle toward a slow recovery. The administrative and financial burdens created by this repeal is a significant stumbling block to our recovery effort.

We appreciate your interest and urge your earliest consideration of this request.

Sincerely,

Joseph M Stevens

Mr. Joseph M Stevens

COMMENTS ON THE IMPACT OF REPEALING THE UP-FRONT DIESEL TAX EXEMPTION

Using repeal of the up-front diesel tax exemption to ensure all taxes on diesel are collected, is tantamount to incurring the expense and effort associated with setting a bear trap to catch a mouse!

Brown & Root is a major user of diesel fuel, virtually all of which is for off road purposes. These uses include heavy equipment (large and small cranes, dirt moving equipment, paving equipment, etc.), marine vessels (barges, supply boats, etc.) and diesel powered machinery of various utilities (e.g. welders, compressors, generators, pumps, etc.)

During 1987, Brown & Root collectively purchased 2.6 million gallons of diesel fuel, of which, conservatively, 95% was for off road use. Had the repeal of the up-front diesel tax exemption been in effect in 1987, Brown & Root would have experienced an additional average monthly cash outflow flow of approximately $30,000 per month. Because a refund for this amount can only be solicited quarterly, the additional interest expense would be in the neighborhood of $4,000 per quarter, based on current rates of interim financing.

Because repeal of the up-front diesel tax exemption will necessitate filing for refunds on a quarterly basis, administrative costs will also increase, i.e. those associated with the filing, as well as distribution of refunds to the numerous divisions, and literally hundreds of jobs. (The latter was not required in the past, as the job only received the "net charge". With the repeal of the up-front diesel tax exemption, monthly accruals of the credit will have to be maintained, with quarterly refunds posted back to those jobs.)

Considering growth projections for 1988, it is reasonable to estimate the interest and overhead expense impact of repealing the up-front diesel fuel purchase exemption at Brown & Root will be $100,000 for the first year.

It is abusive to burden an industry with a "pay not/refund later" type of program, when 95% or more of the amount will be refunded. It adds extra work and cost, and accomplishes very little for the country. And further, the costs associated with this government imposed inefficiency will ultimately come back to the taxpayer in the form of higher prices. Therefore, no one is a winner!

THE CARTER MINING COMPANY
POST OFFICE BOX 3007 • GILLETTE, WYOMING 82716-0607 • (307) 682-8881

D.B. ACHTTIEN
PRESIDENT

March 15, 1988

Ms. Laura Wilcox
Hearing Administrator
U.S. Senate, Committee on Finance
Room SD-205, Dirksen Office Building
Washington, D.C. 20510

Dear Ms. Wilcox:

On behalf of The Carter Mining Company (TCMC), we welcome the opportunity to comment on the recent change in the diesel fuel excise tax collection procedure included as part of the Omnibus Budget Reconciliation Act (OBRA) (P.L. 100-203). TCMC annually purchases millions of gallons of diesel fuel for use in its coal mining operations. Like farmers, coal surface mining companies, such as TCMC, use only a minute portion of the diesel fuel purchased in a taxable manner. Substantially all of the fuel is used off road (an exempt purpose) in the mining operations. However, under the provisions of the 1987 OBRA, TCMC will be required to pay the full amount of the tax even though it ultimately is not liable for taxes and a refund or credit against income taxes paid can subsequently be obtained. Therefore, for the following reasons, TCMC requests that the coal mining industry be allowed to purchase diesel fuel for off-road use tax-free, a purchase similar to those allowed for the railroad and aviation industries.

The impact of the new collection procedure on the coal mining industry in general and TCMC in particular creates an undue economic hardship on an industry that is already burdened by the economic effects of a depressed coal market. Although a refund or credit would be available to diesel fuel users who use fuel in an exempt manner, the payment of the tax will burden companies that purchase substantial amounts of diesel fuel for off-road use in their operations. Financial resources which would ordinarily be used for the production of coal and ongoing mining operations will be channeled to pay the taxes. Further, mine operating expenses will increase due to added interest costs for purchasing the fuel and additional record keeping procedures to enable recovery of the funds once the refund procedures have been established. All of the above results expose TCMC and the coal mining industry to increased economic burdens, further weakening the economic condition of the industry in an extremely competitive environment.

In addition to the economic hardships, policy considerations exist for diesel fuel for off-road use to be purchased tax-free. The expanded refund procedures will require additional compliance costs, as well as IRS auditing costs -- not to mention additional government and taxpayer expense if litigation were involved -- thereby channeling resources away from industrial development.

Thus, given the economic burdens that may be imposed on TCMC specifically and the coal mining industry in general, as well as the policy considerations, we urge the Committee to consider providing the coal mining industry with an exemption to purchase tax-free diesel fuel for off-road use.

Sincerely,

STATEMENT OF

CROWLEY MARITIME CORPORATION

The inclusion in the 1987 Budget Reconciliation Act of provisions (Section 10502) which impose diesel fuel taxes of 15.1¢ per gallon on the producers of the fuel, changing the point of assessment from the retailer, invokes a harsh and unreasonable burden on Crowley Maritime Corporation and most of the maritime industry.

Included in Section 10502 is a special rule authorizing the Secretary of the Treasury, by regulation, to exempt several classes of taxable fuels, to wit:

1. Heating oil
2. Sales to producers
3. Diesel fuel sold for use in diesel-powered trains
4. Aviation fuel sold for use in commercial aircraft
5. Fuel for use other than as a motor fuel
6. Fuel sold to State and local governments.

To those classes should be added fuel sold for use on commercial vessels.

Crowley Maritime Corporation operates over 150 tugs primarily in service between the United States mainland and Alaska, Hawaii, and Puerto Rico and in the coastwise trades. We also operate several liner vessels in international trade. All of the tugs use Marine Gas oil, the equivalent of #2 diesel oil, which we believe fits the definition of taxable fuel set forth in the Act. Liner vessels, in their main engines, use Intermediate Fuel oil and Marine Diesel oil which we believe do not fit the definition of taxable fuel. Liner vessels in their auxiliary engines will,however, frequently use Marine Gas oil (#2 diesel), although some auxiliaries can burn a

blend not suitable for use on the highway. Many liner vessels hold Marine Gas oil in on-board tanks for blending aboard ship with heavier fuels as required.

We estimate that our company purchases for use on our vessels 80,000,000 gallons of diesel fuel annually. For each month that taxes are paid and held by the U.S. government awaiting refund, $1,000,000 of our money is tied-up.[1] Assuming that we pay the tax for three months before submitting the quarterly application for refund and that the IRS requires three months to process the application, we will have $6,000,000. which is lawfully ours, held continuously by the government. We have been told that processing applications, at least initially, could take much longer than three months - perhaps as long as a year to 18 months - which would obviously be a severe financial penalty. Whether processing would take as long as 18 months is not critical to our plea - six months and $6,000,000 is bad enough, and should make our point.

In discussing this matter with Congressional staff we were advised that two criteria were used to exempt railroads and airlines. They were (1) large fuel consumption; and (2) a small number of companies to monitor. We were further advised that the revenue gain to be derived from changing the point of assessment from retailer to producer is comprised of two elements. The first is the loss avoidance associated with reducing the potential for diverting fuel to highway use without payment of tax and the second is the value of holding the taxes collected until such time as they are refunded.

Those criteria and elements may seem appropriate to staff, but they are inappropriate as a basis for discriminating among similarly positioned industries. The basic justification

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1. 80,000,000 gals/yr x 15.1¢ ÷ 12 months, rounded off.

for exemption in the case of diesel fuel must be that the fuel is not used on the highway. Clearly fuel aboard vessels is comparable in that regard to fuel used on railroads. This discrimination between modes is further aggravated because, in the case of tugs used in inland waterways, the railroads and tug/barge companies compete with one another.

It is particularly irritating that it should be suggested that our case lacks merit because, should we prevail, the government would lose the value of holding the taxes collected until refunded.

In addition to the severe adverse effect on cash flow, the administrative problems of recording purchases and submitting refund applications are significant. That portion of fuel purchased in the United States is bought from many sources. Each of our tugs takes fuel on the average of every two weeks, the source dependent on where they may be when fuel is needed. Our liners buy fuel throughout the world. If the administrative problems are large for the industry, it must surely be costly to the government to process and audit the many refund applications they will receive.

The condition of the U.S. maritime industry was described by the Presidential Commission on Merchant Marine and Defense in their report of September 30, 1987. Among their findings was this statement:

> "The maritime industries have been in a state of decline for many years, but the rate of decline is now increasing at an alarming rate. Some of the largest ship operators, shipyards, and shipyard suppliers have gone out of business, and most of those that remain face serious financial hardships.

The Commission's analysis shows that, unless actions are taken to reverse the downward trend, the number of merchant ships and seamen will be reduced by one-half by the year 2000."[2]

As we seek ways to be more competitive, we would hope that our government would not put impediments in our way.

Please add another exemption category - fuel sold for use on commercial vessels.

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2. Page 2, item 7.

ILTA

March 16, 1988

Senator David L. Boren
Chairman, Subcommittee on Energy
and Agricultural Taxation
SENATE FINANCE COMMITTEE
SD-205 Dirksen Senate Office Building
Washington, D. C. 20510

Statement of John Prokop, ILTA
Submitted for inclusion in the Hearing Record
on Collecting Federal Fuel Taxes

Dear Mr. Chairman:

The Independent Liquid Terminals Association is an internationally recognized trade association representing 70 highly reputable companies with more than 320 "for-hire" bulk liquid terminals.

These terminals are bulk liquid warehouses that do not own the products stored there. The business of these for-hire terminals is to lease storage tank space to the owners of a wide range of commercial bulk liquids. These product owners include oil and chemical companies, manufacturers, utilties, government agencies including the Department of Defense, brokers, and transporation companies (airlines, ocean-going vessels, etc.).

As many as 30 ILTA member companies have one or more U.S. terminals that store and transfer gasoline, or blendstocks, or additives, or all three commodity types subject to the federal excise tax. As much as 20 percent of these taxable commodities sold or consumed in the U.S. are handled by ILTA Terminal Members.

For-hire Terminals Concerned About Being Saddled
With Tax Liability of Gasoline Owners Who Evade IRS

These ILTA members are concerned with §1703 of the Tax Reform Act of 1986, amending 26 USC 4081, and with recently issued and proposed regulations.

While one purpose of the Act is to stop gasoline tax evasion by gasoline owners, including proprietary terminal operators who buy and sell gasoline, it also imposes tax liability on "for-hire terminals" if any of their storage customers fail to pay any gasoline excise tax due to the IRS.

This liability attaches under the 1986 Tax Reform Act despite the fact that the for-hire terminal never takes title to or owns the gasoline stored at and transferred to and from the terminal. It never buys or sells gasoline. It is never involved in the financial transaction between the owner and seller of the gasoline. The for-hire terminal usually does not know who purchased or exchanged the gasoline, and, if sold, whether the sale was a tax-free or tax-paid sale. It does not know what the sale price was or whether the gasoline owner-seller/storage customer paid the excise tax on the sale to the IRS or to any state tax collection agency.

A for-hire terminal only stores and transfers the gasoline according to the instructions of the "storer of record."

Nevertheless, the 1986 Tax Reform Act imposes liability on a for-hire terminal for the failure, for any reason whatsoever, of a gasoline storage customer to pay the excise tax it owes to the IRS -- a situation beyond the knowledge and control of the for-hire terminal.

Allegedly, this approach was adopted to prevent any terminal from forming a separate corporation to buy and sell gasoline and evade taxes, and then have that corporation disappear as the IRS became aware that a tax scam was at hand (which can take as long as two years or more). The way the 1986 Act was written, it assumes that all terminal operators are and were guilty of this practice. Yet, the persons who have been arrested for these tax scams were not any of the gasoline owners certificated by the IRS to sell tax-free gasoline or to exchange it, or any companies that are members of any of the reputable terminal trade associations.

Among the reasons ILTA members are concerned about this provision in the law is:

(1) A for-hire terminal does not have to be guilty of anything to be liable to pay someone else's gasoline excise tax; all they need is to have had a gasoline storage customer who, for any reason whatsoever, did not or was unable to pay his gasoline excise tax.

(2) A for-hire terminal earns as much as 1/2¢ per gallon for handling a gallon of gasoline. Its tax liability would be 9.1¢ per gallon for someone else's taxes. This is an unbondable liability for any amount, according to the bonding industry. The consequences to ILTA terminal members could be devastating. For example, ILTA's largest member would have exposure for almost $1 billion of customers' excise taxes, and another would have exposure for excise taxes on 4% of the gasoline consumed in the United States.

This exposure far exceeds a for-hire terminal's financial capability to cover such liability. In a survey of ILTA Members, the potential liability for such taxes averaged 22 times what the companies earned for handling and storing a gallon of gasoline.

(3) The for-hire terminal never knows whether a gasoline storage customer pays its excise taxes to the IRS and state agencies, and has no control over its customers to make them pay the IRS.

(4) Because the IRS has not developed an extensive and comprehensive system to detect and apprehend gasoline tax evaders, the Treasury and IRS wanted for-hire terminal operators to insure or guarantee that they will pay the excise taxes of gasoline storage customers who turn out to be either tax evaders or financially failed companies.

Because of the understandable Congressional difficulty in immediately amending the Tax Reform Act with a Tax Corrections Act to cure such injustices, ILTA and others instead were required to negotiate changes with the IRS in its regulations. The IRS rules, which were not proposed for industry comment, but which were issued as final on November 18, 1987, were effective January 1, 1988. An IRS rules hearing was held on January 5, 1988, to discuss needed corrections.

The IRS informs us that, under the regulations, a for-hire terminal that obtains a copy of a gasoline storage customer's IRS certificate is approved to handle that customer's gasoline and is not liable for any tax evasion that a certificated customer may engage in.

The ILTA, however, is not convinced that the new IRS system cannot still be exploited to evade taxes or to leave for-hire terminals exposed to tax liability that should be exclusively that of unscrupulous tax-evading gasoline owners. If the government's description of the immense illegal profits that can be made is accurate, we fear that this will lure the tax evaders to return with more sophisticated methods of evasion.

If the IRS certificates a new company to buy and sell gasoline, and that company leases storage and transfer services at ten different for-hire terminals, none of those terminals will know whether that company has paid its excise taxes. Suppose the new gasoline seller, as a guise, pays only 40% of the excise taxes and evades payment on 60%.

Because of the lack of an IRS detection system, two years and millions of dollars in evaded taxes later, the IRS gets suspicious, and the nervous tax evader gasoline-owner disappears with his ill-gotten gains. Then, ten IRS-certified for-hire terminals are all that are available for the IRS to pursue under the 1986 Tax Act.

Tax attorneys reacting to past experience have raised these questions for ILTA: Despite the protection interpreted into the IRS rules by the rules writers, will the IRS enforcement division bill these terminals jointly and severally for the taxes that their common tax-evading customer did not remit to the IRS? Will the IRS assume that the for-hire terminals are guilty of aiding and abetting the tax evader and ask them to prove legally that they are not guilty?

We hope that the IRS enforcement office lives up to the interpretations and promises made to ILTA by the IRS division responsible for writing the regulations. Our concern and experience is that, in the future, when the current IRS personnel are not with the agency or are in different positions, will anyone remember what has been promised?

As protection, we have asked that the IRS include a statement in the preamble to its revised regulations (due out April 1, 1988, or later) that clarifies that the for-hire terminal liability for any evaded gasoline excise taxes is limited by a terminal's (1) being proven culpable of aiding a taxpayer to avoid paying the taxes, or (2) being proven to be the actual owner of the gasoline and, therefore, the evading tax-payer.

Thus far, the ILTA is pleased and grateful for the the efforts that the IRS and Treasury have made to undo the many conflicts and injustices imposed by the IRS gasoline excise tax regulations, and to attempt to assure that honest for-hire terminal operators are not unjustly penalized for the violations of others.

Another matter of concern is that a for-hire terminal will still have a tremendous ratio of financial liability for taxes vs. its earnings on a gallon of gasoline for: (1) an error a terminal employee might make, such as forgetting to get a customer's tax certificate number; or (2) handling an operational emergency such as receiving an overflow volume destined for another facility down the pipeline (when that facility was unable to accept its full shipment) and then never getting the storage customer's IRS certificate number for the terminal records.

ILTA feels that if the IRS uncovers a situation where a for-hire terminal employee made such a mistake, and it was not part of a deliberate tax evasion scheme, the terminal should be made to pay a reasonable penalty for its negligence or oversight, but it should not have to reimburse the IRS for the excise taxes. That tax liability should be exclusively that of the gasoline owner/storage customer, even if, subsequently, the company is unable to pay the taxes or has gone out of business.

While for-hire terminals have expressed many concerns about the regulations to the IRS, and they hope the forthcoming IRS revisions will resolve these concerns, they wish to state also, for the record of Congressional Committees, their gravest concern, which is this potential exposure for customers' gasoline excise taxes.

We also wish to call to your attention, as we are sure the IRS already has, that, under the current law, it is not legal for the IRS to tell a for-hire terminal whether the owner of the gasoline-tendered-for-storage holds an IRS certificate (to sell gas tax-free, make exchanges, etc.). This law needs to be changed to aid both the IRS and for-hire terminals in determining whether a gasoline owner's gasoline can be accepted into commerce for distribution and sale.

Since gasoline tax evasion by criminal elements, as well as by small time tax evaders, poses a threat to both honest proprietary gasoline owners and for-hire terminal operators, the ILTA supports the Congress, the Department of Treasury, and the IRS in this effort to stop tax evasion. We share the sentiments of other representatives of the petroleum industry and express our willingness to participate in joint government-industry efforts to develop a workable tax collection system which does not injure the honest taxpayers and which apprehends tax evaders.

Thank you for affording us this opportunity to submit comments for the record.

Sincerely yours,

John Prokop

John Prokop
President and General Counsel

rdm

ILTA TERMINAL MEMBERSHIP *

(as of March 16, 1988)

1. Allied Terminals, Inc.
Aviation Fuel Terminals, Inc.
Brasterminais Armazen Gerais Ltda.
C. Brewer Terminals, Inc.
5. Buckeye Tank Terminals, L.P.

Bulk Storage Terminals, Ltd.
Cargill, Inc.
Colonial Terminals, Inc. *
Columbia Terminals
10. Coogee Chemicals (Pty.) Ltd.

Croda Storage, Inc.
Delta Commodities, Inc.
Demaco Corporation
Ergon, Inc. *
15. Fuel Storage Corp.

Gardner Smith Proprietary, Ltd.
GATX Terminals Corp.
Gordon Terminal Service Co.
Gulf Interstate Energy, Inc.
20. Hitchcock Terminal Services, Inc.

Houston Fuel Oil Terminal Co.
Hudson Tank Terminals Corp.
Intercontinental Terminals Co.
International Matex-Tank Terminals
25. Intertank

ITAPCO
Lake River Corp.
The Lemm Corporation-Operations
Montank Transit Inc.
30. New Haven Terminal, Inc.

NOCO Energy Corp. *
Norfolk Oil Transit, Inc.
Northville Industries Corp. *
Oiltanking, Inc.
35. Pacific Molasses Co.

Paktank Corporation
Panocean USA Inc.
Peerless Oil & Chemicals, Inc.
Petro-Diamond Terminal Co.
40. Petroport Terminal Corp.

PetroUnited Terminals, Inc.
Port of Port Royal, Inc.
Powell Duffryn Terminals Inc.
Public Terminals, Inc.
45. Queen City Terminals, Inc.

Raj Chemicals of Va., Inc.
Richards Bay Bulk Storage (Pty.) Ltd.
River Transportation Co.
Rowell Chemical Corporation
50. Seaview Petroleum Co.

South Coast Terminals, Inc.
Southern Pacific Pipe Lines
Statia Terminals
Steuart Petroleum Company *
55. Stolt Terminals, Inc.

ST Services
Terminales Quimicos De Puerto Cabello, C.A.
Tidewater Terminal Company
Time Oil Co. *
60. Tri-Central Marine Terminals, Inc.

Unitank Terminal Service
Valleytank, Inc.
Venterminales
W.A.S. Terminals, Inc.
65. Westway Trading Corp.

Whitaker Oil Company *
Williams Pipe Line Co.
Wilmington Liquid Bulk Terminals, Inc.
69. Wolf Lake Terminals

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* A few terminals are proprietary, but also have a substantial for-hire storage and transfer business; ILTA represents only their for-hire interests.

STATEMENT OF
INDEPENDENT PETROLEUM ASSOCIAITON OF AMERICA
AND

AMERICAN ASSOCIATION OF PETROLEUM LANDMEN
ASSOCIATION OF OILWELL SERVICING CONTRACTORS
CALIFORNIA INDEPENDENT PRODUCERS ASSOCIATION
COASTAL OIL AND GAS ASSOCIATION
EASTERN KANSAS OIL AND GAS ASSOCIATION, INC.
EAST TEXAS PRODUCERS AND ROYALTY OWNERS ASSOCIATION
ENERGY CONSUMERS AND PRODUCERS ASSOCIATION
GEORGIA OIL AND GAS ASSOCIATION
ILLINOIS OIL AND GAS ASSOCIATION
INDEPENDENT OIL AND GAS ASSOCIATION OF NEW YORK
INDEPENDENT OIL AND GAS ASSOCIATION OF WEST VIRGINIA
INDEPENDENT OIL PRODUCERS' AGENCY
INDEPENDENT OIL PRODUCERS ASSOCIATION TRI-STATE, INC.
INDEPENDENT PETROLEUM ASSOCIATION OF MOUNTAIN STATES
INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO
INDIANA OIL AND GAS ASSOCIATION
INTERNATIONAL ASSOCIATION OF DESK AND DERRICK CLUBS
INTERNATIONAL ASSOCIATION OF GEOPHYSICAL CONTRACTORS
KANSAS INDEPENDENT OIL AND GAS ASSOCIATION
KENTUCKY OIL AND GAS ASSOCIATION
LIAISON COMMITTEE OF COOPERATING OIL AND GAS ASSOCIATIONS
LOUISIANA ASSOCIATION OF INDEPENDENT PRODUCERS AND ROYALTY OWNERS
LOUISIANA LANDOWNERS ASSOCIATIONS, INC.
MICHIGAN OIL AND GAS ASSOCIATION
NATIONAL STRIPPER WELL ASSOCIATION
NEW MEXICO O[illegible] AND GAS ASSOCIATION
NEW YORK STA[illegible] OIL PRODUCERS ASSOCIATION
NORTH TEXAS OIL AND GAS ASSOCIATION
OHIO OIL AND GAS ASSOCIATION
OHIO PETROLEUM PRODUCERS ASSOCIATION
OIL INVESTMENT INSTITUTE
OKLAHOMA INDEPENDENT PETROLEUM ASSOCIATION
ORANGE COUNTY PETROLEUM ASSOCIATION
PANHANDLE PRODUCERS AND ROYALTY OWNERS ASSOCIATION
PENNSYLVANIA GRADE,CRUDE OIL ASSOCIATION
PENNSYLVANIA NATURAL GAS ASSOCIATES
PENNSYLVANIA OIL AND GAS ASSOCIATION
PERMIAN BASIN PETROLEUM ASSOCIATION
ROCKY MOUNTAIN OIL AND GAS ASSOCIATION
ROYALTY OWNERS AND INDEPENDENT OIL AND GAS PRODUCERS ASSOCIATION OF ARKANSA
TENNESSEE OIL AND GAS ASSOCIATION
TEXAS INDEPENDENT PRODUCERS AND ROYALTY OWNERS ASSOCIATION
VIRGINIA OIL AND GAS ASSOCIATION
WEST CENTRAL TEXAS OIL AND GAS ASSOCIATION

On behalf of the Independent Petroleum Association of America (IPAA) we wish to comment on the proposed changes in the diesel fuel tax collection procedures. Together with the 44 unaffiliated state and regional associations listed on the cover page, we represent the estimated 12,000 independent oil and gas producers who account for 90 percent of the wildcat drilling in the United States and 85 percent of all drilling, which results in a majority of the significant oil and gas discoveries.

Independent producers are directly impacted by the change in the collection of the 15.1 cent excise tax on diesel fuel. This change in the collection procedure was caused by the enactment of the Omnibus Budget Reconciliation Act of 1987. As the law currently stands, off-road users of diesel fuel (e.g. drilling rig operators) will have to pay the 15.1 cent per gallon levy to the IRS and apply for a refund of the tax. In accordance with the law, no interest is paid on the refund. This procedure must

be followed in spite of the fact that almost all these users are exempt from the tax. This roundabout collection method results in an interest-free loan to the government and a devastating cash impact on these exempt users.

For instance, the Association of Oilwell Servicing Contracts estimates that their members would have to pay $23,500,000 per year to the IRS under this provision, but they would only owe $1,173,500 in actual taxes. Independent oil and natural gas producers are directly and indirectly affected by this provision. Our members who own drilling or well servicing rigs will have to pay the tax and apply for a refund. Other members will be affected indirectly through higher drilling costs in the form of interest expense or uncollected refunds being passed on to them. This increase in costs will be disastrous at a time when the industry can least afford it.

We don't believe that the IRS has demonstrated any perceived abuses under the current system of collection. In fact, very little justification for the change in collection procedure has been offered, except general statements that revenue-losing abuses have occurred.

This fact can be further amplified by the revenue loss estimates prepared by the Joint Committee on Taxation:

Fiscal Year Revenue Increase (in millions)

	1989	1990	1989-1990
1) Diesel Fuel Proposal as originally adopted	$230	$200	$430
2) Diesel Fuel Proposal as modified due to lost interest	(305)	(58)	(363)
Differences due to compliance abuses	$<75>	$142	$67
	=====	=====	======

It would appear from these figures that approximately 85% of the revenue projected for the original provision results from an interest-free loan to the government and not from compliance problems. We think that this is an absurd result. Operators of drilling and workover rigs should not be required to give the government an interest-free loan of taxes they don't owe.

IPAA recommends that Congress rectify this problem by adding a fifth category of fuel that is exempt from the tax. This category would be off-highway use and there could be a certification procedure whereby drilling rig operators and well service rig operators would qualify to purchase diesel fuel tax-free. The provision would not diminish the original intention of the 1987 change or result in a significant revenue loss. If you have any questions concerning this statement please feel free to call our Resident Tax Specialist at 857-4734.

STATEMENT OF THE
NATIONAL ASSOCIATION OF TOWNS AND TOWNSHIPS
For the Record of the
Senate Finance Committee
Subcommittee on Energy and Agricultural Taxation

March 16, 1988

This statement is submitted on behalf of the National Association of Towns and Townships (NATaT) which represents over 13,000 units of general purpose local government across America. These mostly small, mostly rural communities are typical of the majority of the 39,000 local governments in the United States, Mr. Chairman, 72 percent of which represent populations under 3,000.

In fact, half of all the general purpose governments in America -- counties, municipalities, towns and townships -- are communities of less than 1,000 people. It is these communities, these governments and the volunteer local officials who administer them, that we need to think about today as we consider the implications of recent changes to the federal gasoline tax exemption procedure.

Historically, Mr. Chairman, small businesses have been afforded a measure of protection through legislative and regulatory approaches which acknowledge that too many rules can sink a small business. What needs to be recognized is that small communities across America are in that same leaky boat. They need the same kind of protection to stay afloat during this very difficult time.

Over the past several years the federal government has withdrawn almost all support for small town America, and has left it to fend for itself. With the loss of General Revenue Sharing, 80 percent of all governments have no ties with the federal government in terms of funding; no grants, no loans, no revolving funds, no programs of any kind. What remains is a disconcerting, growing burden of rules, paperwork, and mandates.

At the same time, the relationship between the federal, state and local governments is changing. No longer are small governments looked on as partners in implementing federal policy at the local level; but rather they are seen as just another "interest group," competing with the public and the private sectors for recognition. And not only that, Mr. Chairman, but now they are beginning to be viewed as a revenue source for federal funds!

If the Congress truly thinks that there is money in small town governments to help the federal treasury, there is clearly a breakdown in communication. On one hand, Congress appears to recognize the crisis situation in rural areas -- employment is down, property values are down, the infrastructure is crumbling even as we speak-- and there appears to be a real awareness that small town America is in trouble. But then along comes an initiative such as the gasoline exemption issue which needlessly adds to the problems of these already overburdened localities.

Mr. Chairman, small towns are just not prepared for this situation. In the first place, they didn't budget for these up-front payments of gasoline taxes. Although the amounts are small in federal government terms, they are fairly sizeable in terms of small town budgets. A recent, informal poll of NATaT members revealed that responding town and townships governments representing less than 1,000 people had an average annual budget of $55,000 to run the whole town. And now Congress says, "Send us some of that money. We know you don't owe it, but send it anyway, and we'll keep it for a while and make interest on it and send it back some other time."

In the second place, there is the issue of how much this is costing in terms of labor and paperwork for small town governments? We are talking about 28,434 governments, all of which have populations of less than 3,000 people, filing returns at least once a year if not quarterly. Add another 10,000 governments -- those with more than 3,000 people, and you have a massive paperwork burden on both ends.

And how will IRS respond to this influx of new demands? Although we do not have access to hard data, it is our understanding that refunds in other instances can take up to several years. What mechanism is in place to insure a timely response on the part of IRS? Perhaps the committee should consider placing a penalty on the agency for failure to respond in a timely manner, in order to provide an incentive for a quick turn-around. Otherwise, what is to prevent Treasury from keeping state and local funds for an inordinate time, since the interest they will be making on state and local money has clear budgetary implications.

There are some -- unfamiliar with small towns -- who may say "those governments won't even file for a refund, the dollars are so small." Mr. Chairman, that's just wrong. Local volunteer officials can do more with less money than just about anybody else I know, and even small amounts of money mean a great deal to small governments. The poll I referred to earlier asked NATaT members to say

what they could do with $5,000 -- how their government would use that money. The results are quite illuminating.

Local officials in Wakita, Oklahoma, for example, could puchase new bunker uniforms for their volunteer fire department with $5,000. Such uniforms are mandated by new Superfund legislation, Mr. Chairman, and Wakita isn't sure right now where they will get that money.

Graceland Township in South Dakota is typical of governments which would use $5,000 to replace aged bridges which cannot sustain today's heavy vehicles.

Agua Dulce, Texas, could fix water lines, sewer lines, or upgrade its fire hydrant system. Santa Fe would turn on 20 street lights for one year.

Woodland Township in Michigan could contract for ambulance service for one year; Bath Township could pay the entire equipment costs for one year for its fire department.

And Colgate Township, North Dakota, could pay the salaries of all elected officials for ten years with $5,000!

Communities such as these will be filing for refunds -- of taxes, may I reemphasize, that they *do not owe*.

Furthermore, we believe that this situation invades the traditional reciprocal tax-exempt relationship among federal, state and local governments, and entirely ignores the interdependent network of cooperation which must exist among these entities.

The Board of Directors of the National Association of Towns and Townships met this week in Washington to pass a resolution reemphasizing that local governments must continue to enjoy the same immunity from federal taxation as the federal government enjoys from taxation by local government entities. The resolution also calls upon Congress to amend current law which abrogates this relationship.

I urge you to do just that, Mr. Chairman. Your committee has an opportunity right now to stand up for small town America and for the traditional federal-state-local government relationship, by restoring to state and local governments their exemption from federal gasoline excise taxes at the point of sale. But before that,

we urge the full committee to hold additional hearings on this issue. There are grave implications, as we have pointed out, in this precipitous and drastic change in the federal-state-local relationship which cannot be adequately addressed in this short time frame.

At the very least, Mr. Chairman, I urge the committee to give small governments the same kind of support that Congress affords to small businesses in other instances, by amending the legislation under consideration to exempt local governments with populations below 3,000 from these provisions.

March 14, 1988

National
Council of
Farmer
Cooperatives

The Honorable David L. Boren
Chairman
Subcommittee on Energy and Agricultural Taxation
Committee on Finance
United States Senate
Washington, D.C. 20510

RE: DIESEL FUEL EXCISE TAX COLLECTION PROCESS

Dear Mr. Chairman:

The National Council of Farmer Cooperatives (National Council) is pleased to submit comments concerning changes in the diesel fuel excise tax collection process as they impact upon the American farmer.

Interest of the National Council

The National Council is a nationwide association of cooperative businesses which are owned and controlled by farmers. Its membership includes 91 major marketing and farm supply cooperatives, the 37 banks of the Farm Credit System, and 33 state councils of farmer cooperatives. National Council members handle practically every type of agricultural commodity produced in the U.S., market these commodities domestically and around the world, and furnish production supplies and credit to their farmer members and patrons. Five out of six U.S. farmers are affiliated with one or more cooperatives. The National Council represents about 90 percent of the nearly 5,800 local farmer cooperatives in the nation, with a combined membership of nearly 2 million farmers.

Among the farmer cooperatives the National Council represents are supply cooperatives which own and operate five efficient refineries possessing an aggregate production capacity of 337,700 barrels per stream day. Cooperatives market petroleum products in more than 40 states and currently supply about 40 percent of all on-farm fuel and a large portion of rural needs.

Farmer cooperative petroleum operations represent the only segment of the oil industry in which the consumers of its products are also its owners. This feature carries with it a unique accountability in terms of commitment of supply, service and price.

50 F Street, NW
Suite 900
Washington, DC 20001
202/628-6676

Serving America's Family Farmers

The Problem

The American farmer has been able to make tax exempt purchases of diesel fuel for farm operations and other off-highway uses ever since the highway use tax at the federal level was established.

When Congress enacted the Budget Reconciliation Act, it included a provision that moved the point of taxation from the retail level to the last wholesale level. As we understand it, the objective was to reduce or eliminate tax evasion, particularly at truck stops. Congress also eliminated a number of exempt purchase categories, including that for farmers, while allowing the IRS to continue exemptions on a case-by-case basis for railroads, airports and state and local governments. There is no such discretionary authority for the farm community.

This change means that farmers will have to pay the excise tax on all diesel fuel purchases, regardless of intended use, effective April 1, 1988--absent timely action by the Congress and/or the IRS. The price paid will increase by 15 cents per gallon.

Farmers will have two basic options for reimbursement of taxes paid which they do not owe:

1. A credit on one's income tax return (1040); or

2. A direct refund, up to a quarterly basis over the first nine months of any year, if the liability exceeds $1,000.

In economic terms, this means that the IRS is securing an interest free loan from farmers, starting from the time the tax is paid to the point at which a refund or credit occurs. Realistically, only the larger farms will have the option of exercising the direct refund option. In most instances, cash that is badly needed to defray ongoing expenses of farm operations, or of farm family needs, will be transferred from farmers to the coffers of the IRS.

Depending upon one's assumptions, the time cost of money denied farmers could range from $6 million to $25 million annually. Should states later mirror the federal legislation in their tax collection practices, as expected, the total impact could be up to 40 percent greater.

The National Council anticipates that the local cooperative will qualify as a wholesaler for the purpose of assessing the highway use tax on diesel fuel, in that local cooperatives make bulk deliveries to storage tanks on farms. Local cooperatives have also served as retailers responsible for collecting the same excise tax under laws in effect up to this point. Thus, the new tax change is expected to have only minimal effect upon tax collection points in the cooperative petroleum supply system.

Over the years, we believe that cooperatives and their farmer customers have established a good track record in distinguishing between off-highway (exempt) use of diesel fuel and those purchases for on-highway transportation. Indeed, the IRS recognized in proceedings last year that the recordkeeping system of petroleum cooperatives at self-service, "Cardtrol/Keytrol" stations had sufficient quality control to permit both taxable and nontaxable sales to farmers through those outlets.

Thus, the National Council does not believe that the congressional objective of reducing tax evasion—an objective which we wholeheartedly support—would be furthered in any way by forcing farmers to pay a tax which they do not owe on their major power fuel, and then seek a credit or a refund up to a year later. The major impact of this new procedure is more likely to be a paperwork nightmare for both the farm community and the IRS. The dollar costs of that burden surely would more than cancel out any diminimus improvement possible in tax compliance.

Recommended Action

It is most unfortunate that the IRS has concluded that it has no flexibility under existing law to suspend the effective date of this change until such time as Congress can complete its work. It makes little sense for the agricultural community, the rural petroleum supply system and the IRS to go through the extensive time and costs involved in implementing this change, only to reverse the process a few months later.

Accordingly, the National Council has been urging the Congress to act to restore the farm exemption from the highway use tax on diesel fuel as quickly as possible. We are most pleased that the Finance Committee has scheduled markup for March 18.

We would respectfully request that this letter be incorporated as part of the record of the March 16, 1988 hearing before this subcommittee on the diesel fuel excise tax issue. The National Council and its members stand ready to assist in bringing this problem to a successful and timely resolution.

Sincerely,

R. Thomas Van Arsdall

R. Thomas Van Arsdall
Vice President
Agricultural Inputs and Services

RTVA/kf

cc: Sen. Lloyd Bentsen, Chairman, Finance Committee
Members, Subcommittee on Energy and Agricultural Taxation
Members, Senate Finance Committee

March 16, 1988

The Honorable Lloyd Bentsen
Chairman
Senate Finance Committee
United States Senate
Washington, DC 20510

Dear Senator Bentsen:

The National Fisheries Institute (NFI) appreciates the opportunity to submit testimony in support of S. 2128, Senator Warner's bill to reinstate the up front diesel fuel tax exemption on purchases of fuel for fishery vessels. NFI is a trade association comprised of over 1,000 companies engaged in the harvesting, processing, distribution and sale of fish and seafood products.

The legislation, S. 2128, amends a provision in the Budget Reconciliation Act of 1987 which changed the collection point of the 15.1 cent per gallon diesel fuel excise tax from the retail to the wholesale level. That change adversely impacts the U.S. fishing industry. Senator Warner and the cosponsors of S. 2128 recognize this burden and offer a solution that fishermen, who are clearly purchasing fuel for marine use, not be required to pay a tax that is not owed.

Although under current law refunds can be obtained, fishermen will still suffer from the loss of an up front exemption. Fuel costs are a major, often the single most significant, operating expense for vessel operators. There are roughly 130,000 fishing vessels and boats in the U.S. at the present time. Many are owner operated, most other vessels are part of small fleets. Vessel owners are small businessmen and women who are being asked to accept an increase in fuel costs of approximately 20 percent and provide the federal government with an interest free loan.

Already, maintaining a steady cash flow is difficult given the nature of the fishing industry. Factors beyond the fishermen's control including, weather, fishery management regulations, and natural environmental occurrences, restrict fishing operations to certain seasons. Few vessels fish year round. Fishermen are not guaranteed a predictable income. Catch rates and prices fluctuate from year to year.

Fishermen are guaranteed certain expenditures, however. Payrolls must be met, fishing gear repaired or replaced, and boat repairs are necessary. As a result, many fishermen are forced to operate on a narrow margin or borrow from financial institutions to maintain the necessary capital for vessel operations. Paying unowed taxes exacerbates this plight.

In addition to the financial loss, there is also an administrative burden. Small businesses are already burdened with numerous mandatory paperwork requirements imposed by State, local, and Federal authorities. Unless S. 2128 is enacted, tens of thousands of fishermen will have yet another form to file--quarterly or annually--requesting refunds.

It is possible that the current law effective April 1, 1988 as it applies to the fishing industry will actually cost the federal government money. The budget reconciliation provision was adopted to meet concerns that some highway users were not paying the excise tax. The compliance issue, however, should not involve the fishing industry. First, there is little vertical integration in the U.S. fish and seafood industry. Those engaged in the harvesting sector are not generally involved in the processing or distribution sectors. Harvesters purchasing fuel have no use other than marine use for diesel fuel. Wholesale fuel buyers engaged in fishing operations simply have no reason to divert fuel to highway uses.

Retail sales similarly do not present a compliance problem. There are obvious restrictions as to where vessels can be refueled. Fuel pumps must be located at a dock. It is evident that retail fuel sales to fishery vessels are strictly for marine use.

In short, tax compliance problems that might exist for other industries do not apply to the fishing industry. Therefore, the additional paperwork requirement is not likely to yield additional tax revenues. The processing of refund applications by the Internal Revenue Service, however, will result in some additional administrative cost to the government.

The only likely positive revenue effect will be the interest earned on the fishermen's money by the government. And that raises the issue of fairness. Collecting interest off money that is not owed the government is not fair to the taxpayer. There are more appropriate measures for attaining better tax compliance and NFI urges Congress to consider the alternatives.

For the above reasons, we urge the Senate Finance Committee to favorably act upon S. 2128. The legislation corrects the unintended, unfortunate impacts of the diesel fuel tax provision adopted by Congress last year.

Once again, thank you for allowing NFI to submit comments for the record. Your consideration of our position is appreciated.

Sincerely,

Jim Gilmore

Jim Gilmore, Director
Congressional Relations

national grange

1616 H STREET, N.W. WASHINGTON, D.C. 20006 (202) 628-3507

Robert M. Frederick, Legislative Director

March 11, 1988

The Honorable David L. Boren, Chairman
Energy and Agricultural Taxation Subcommittee
Senate Finance Committee
453 Russell Senate Office Building
Washington, D.C. 20510-3601

RE: Collection Procedures on Gasoline, Diesel and Special Motor Fuel Tax Hearing before the Senate Finance Subcommittee on Energy and Agricultural Taxation on Friday, March 18, 1988

Dear Mr. Chairman:

In recent weeks, a provision in the Budget Reconciliation Act of 1987 has created a tremendous uproar across the country. The provision referred to changed the collection point for the diesel excise tax from the retail level to the wholesale level (Title X, Subtitle E, Part I, Section 10502). The new law will require previously tax-free purchasers to pay the excise tax at the time of purchase and then file for a refund on a quarterly or annual basis.

Although agricultural producers will retain the tax-free treatment for off-highway use, farmers and ranchers will be required to bear up front costs of approximately $420 million a year due to this provision. These additional costs will create cash flow problems for producers and in many cases, will force the farmer to borrow operating capital to pay the tax. Of course, additional loan principal means increased interest payments while the government uses the agricultural producer's money interest-free.

Time is of the essence. The law goes into effect April 1, 1988. Quick Congressional action to repeal this law will remove the tremendous amount of confusion and paperwork which will occur between agricultural producers and the IRS if this provision takes effect. Three bills have been introduced in the Senate which would permit farmers to continue purchasing diesel fuel tax-free for off-highway use. They are S. 2003, introduced by Senator Phil Gramm, S. 2067, introduced by Senator Kent Conrad, and S. 2075, introduced by Senator Tom Daschle. While the legislative language of these bills may vary some, each of them would repeal this nightmare. It is essential that a "clean" bill is placed on the President's desk by the end of March.

This provision will have a significant negative effect on the agricultural economy. On behalf of the over 365,000 members of the National Grange, we encourage the Subcommittee on Energy and Agricultural Taxation and the full Senate Finance Committee to assist in moving this legislation in a most rapid fashion.

Thank you.

Sincerely,

Robert M. Frederick

Robert M. Frederick
Legislative Director

RMF/mnh

STATEMENT OF THE
NATIONAL POTATO COUNCIL

REGARDING FEDERAL EXCISE
TAXES ON FUEL

The National Potato Council (NPC) is the only trade association representing the nation's 12,000 potato growers in thirty-seven states in legislative and regulatory affairs. The following comments reflect the position of the NPC with regard to recent developments concerning federal excise taxes.

The Revenue Act of 1987 (P.L. 100-201) amended Chapter 32 of the Internal Revenue Code of 1986 by adding new Sections 4091, 4092, and 4093. This amendment changed the excise tax on diesel fuel from a retailers' excise tax to a manufacturers' excise tax. As a consequence of this amendment, farmers may no longer purchase tax free diesel fuel for use on their farm for farming purposes.

Before the Revenue Act of 1987 ("Act"), a retailers' excise tax was imposed on diesel fuel either (i) when the fuel was sold and placed into the fuel tank of a highway vehicle, or (ii) when it was used in a highway vehicle if no tax was imposed when it was sold. A farmer could purchase diesel fuel tax free if the dealer delivered the fuel into the farmer's storage tank(s), as distinguished from delivery into the tank of a vehicle. Farmers were exempt from the excise tax on diesel fuel to the extent the fuel was sold for use or used on a farm for farming purposes. If diesel fuel was used for other than farming purposes, the farmer was liable for the excise tax. Thus, if a farmer purchased diesel fuel tax free, but did not use a portion of it for farming purposes, the farmer would be liable for the excise tax on such portion, and would be required to file a Federal Excise Tax Return and pay the tax due. Alternatively, the farmer could purchase diesel fuel subject to the tax, and thereafter claim a refund or a credit against the income tax for the amount of tax paid on the diesel fuel used for farming purposes.

By changing the excise tax on fuel from a retailers' excise tax to a manufacturers' excise tax, the Act advances the point in the chain of sale at which the tax must be collected. After March 31, 1988, the effective date of the new provisions, farmers will either have to pay the excise tax at the time they purchase the diesel fuel or purchase diesel fuel upon which the tax has already been paid, thereby increasing the price of the diesel fuel. Although the new changes require farmers to pay the excise tax on the purchase of the diesel fuel, farmers may claim a credit or refund for tax paid on diesel fuel used on the farm for farming purposes. Generally, farmers must claim a credit for tax paid against their Federal income tax. However, if a farmer is entitled to a refund of $1,000 or more for tax paid during any of the first three quarters of his taxable year, the farmer may claim a refund of the tax paid during such quarter.

In order to prevent taxpayers from purchasing large quantities of diesel fuel before April 1, 1988, thereby avoiding the payment of the tax on that diesel fuel, the Act imposes a Floor Stocks Tax on diesel fuel held on April 1, 1988. The Floor Stocks Tax is imposed at the same rate of tax which would be imposed if the diesel fuel were sold on April 1, 1988. For example, if a farmer had 1,000 gallons of diesel in

a storage tank on April 1, 1988, the Floor Stocks Tax would be $151.00. There is an exception to the Floor Stocks Tax for diesel fuel held "exclusively" for a nontaxable use, such as use on a farm for farming purposes. The key to this exception is the word "exclusively," and it is not known how the Internal Revenue Service will interpret this term. Thus, this exception may not apply if a farmer holds any diesel fuel for a taxable use.

These new provisions impose a substantial financial burden on farmers in two important respects. First, farmers will have to use limited resources to pay a tax for which they ultimately are not liable. In some cases, they will not be able to recover the tax paid for more than 15 months. For example, tax paid on diesel fuel purchased in January 1988 may not be recovered until it is claimed as a credit against the farmer's 1988 Federal income tax return, which would not be due until April 15, 1989. This situation is exacerbated by the fact that the farmer is not entitled to any interest on the refund. Second, many farmers will be subject to a substantial Floor Stocks Tax, which they may not have anticipated when they purchased the diesel fuel.

The National Potato Council shares Congress' general concern regarding compliance with Federal tax laws. Potato farmers understand that they, together with all other honest taxpayers, ultimately bear the economic burden of lost revenue due to taxpayer noncompliance. The methods adopted to address taxpayer compliance problems, however, must be carefully chosen. Taxpayer compliance, although a desirable end, must not be obtained through overly burdensome means. The added expense to farmers and the Federal government caused by requiring farmers to pay the diesel fuel excise tax and claim a credit or refund surely outweigh any added revenue gained. This is clearly a case in which the end does not justify the means. For these reasons, the National Potato Council strongly urges Congress to amend Section 4091 to reinstate the exemption for farmers.

Mr. Larry Young
President
Ron Walker
Executive Director
National Potato Council
9085 E. Mineral Circle
Suite 155
Englewood, CO 80112
(303) 790-1141

Mr. Jerry C. Hill
Mr. Douglas W. Charnas
Counsel
Ms. Tracy L. Smith
Government Relations Advisor
Heron, Burchette, Ruckert & Rothwell
1025 Thomas Jefferson Street, N.W.
Suite 700
Washington. D.C. 20007
(202) 337-7700

Statement of

The National Stone Association

The National Stone Association represents 423 firms that produce crushed stone or manufacture equipment used in such operations. The crushed stone produced by our members is included in the concrete used in constructing our nation's buildings, highways, and industrial and municipal-utility facilities and in the asphalt for highways, parking lots, driveways, and walkways. A substantial portion of the crushed stone produced by NSA members is used for agricultural purposes, erosion control, railroad ballast and environmental applications. Stone, in short, is indeed a ubiquitous national resource.

The National Stone Association welcomes this opportunity to comment on the need for corrective action to restore the up-front diesel fuel tax exemption for off-highway purposes. NSA commends the Chairman and the members of the Committee for the leadership they have shown in holding these hearings and in introducing legislation that would restore the up-front diesel fuels tax exemption allowed under law prior to the passage of the Omnibus Budget Reconciliation Act of 1987.

Mr. Chairman, as an industry composed primarily of small firms, the repeal of the up-front diesel fuel tax exemption imposes a significant burden on crushed stone producers. The crushed stone industry is a capital and energy intensive industry which employs large bucket loaders, bulldozers and over-sized trucks that haul stone from the working face of the quarry to the primary crushers. All of these operations take place within the confines of the quarry; very few of our members own on-highway haulers, as most of them contract out such work to independent contractors.

Simply put, Mr. Chairman, under the law in existence prior to the Budget Reconciliation Act of 1987, only that diesel fuel consumed by on-highway vehicles was subject to the federal excise tax. Conversely, diesel fuel consumed in off-highway operations, such as construction, quarrying and agriculture, among others, was exempt from the tax.

The rationale for adopting this dichotomous approach lies in the principle of the user-fee system which serves as the funding mechanism for the Highway Trust Fund: that the users of the nations's highways, roads and bridges should pay a predetermined share of the construction and repair cost of this vital component of our infrastructure. Because off-highway uses do not contribute to the wear and tear of our roads and bridges, vehicles employed in such operations were totally exempt from the tax.

The Budget Reconciliation Act of 1987 changed the existing law by eliminating, effective April 1, 1988, the off-highway diesel fuel tax exemption requiring crushed stone producers to pay an up-front 15.1 cents per gallon diesel fuel tax to the federal Treasury. Following the payment of the up-front diesel fuel tax, these same producers will be allowed to recover the money paid into the Treasury after filing an application documenting that the fuel was consumed in a non-taxable use.

Mr. Chairman, it is apparent to us that the provision of law implementing this change was singularly ill-considered. The effect of the up-front diesel fuel tax on crushed stone producers is threefold: 1) it imposes an additional and unforeseen production cost on existing supply contracts; 2) it will require additional record-keeping and paperwork to prepare the applications for refunds; and, 3) it will result in the loss of investment income or time value of the funds paid for the tax.

The impact of this change in the tax law on the cash flow of crushed stone producers is significant. For example, one of our member firms, B.L. Anderson, Inc. located in Iowa, used 266,844 gallons of diesel fuel in 1987 for off-highway purposes. The imposition of the 15.1 cents per gallon tax on this particular firm will result in a cash flow loss of $40,293 for that year. Another, much larger member firm, which used 14,000,000 gallons of diesel fuel in 1987 in its off-highway quarrying operations would be required to pay over $2,000,000. On existing contracts, these losses will have to be absorbed by the firm.

The proponents of the up-front diesel fuel tax argue that refunds will be provided by the Treasury Department and will therefore result in no hardship. However, it is very likely that the Department will adopt a quarterly refund schedule which is likely to result in processing delays and the retention of funds without any compensation for the loss of interest which could otherwise have been earned on these funds.

Mr. Chairman, NSA is aware and fully supportive of the need to close the loopholes in our tax laws that allow anyone to avoid paying the taxes they rightfully owe. However, the system adopted by the Budget Reconciliation Act strikes us as draconian and entirely unnecessary.

The Budget Act, by its own terms, requires firms to pay taxes for wholly legitimate non-taxable activities and to subsequently recover their monies through a yet-to-be established refund mechanism -- again without any restitution for loss of interest. The same Act, oddly enough, carves out four exceptions for diesel fuel used for locomotives, commercial aviation, industrial purposes or by states or political subdivisions thereof. For any of these categories, the Act

empowers the Treasury to grant an exemption from the up-front diesel fuel tax following a case-by-case review.

The National Stone Association takes strong exception to this approach and finds it repugnant to any sense of fair play that preferential treatment is given to activities in these four categories while it is denied to our industry and all others. Where is the equity in this? If the case-by-case exemption process is deemed to be a sufficient safeguard to the perceived potential for wrongdoing, it should be extended to all industries and not limited to a preselected few that have no superior claim of legitimacy for their particular non-taxable use.

In conclusion, Mr. Chairman, the National Stone Association urges Congress to take corrective action and restore the diesel fuel tax exemption for the crushed stone industry and for all others that have a legitimate non-taxable use. Again, Mr. Chairman, we applaud your leadership in this matter and we look forward to working with you and the other members of the Committee on this pressing issue.

PACIFIC SEAFOOD PROCESSORS ASSOCIATION
4019 - 21st Ave. West, Suite 201
Seattle, WA 98199
(206) 281-1667
FAX (206) 283-2387

March 11, 1988

The Honorable David L. Boren
Senate Finance Committee
Subcommittee on Energy and Agricultural Taxation
205 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Senator Boren:

I am writing on behalf of the member companies of the Pacific Seafood Processors Association. The Association is submitting this letter for inclusion in the record of your hearing on the collection of federal fuel taxes.

Pacific Seafood Processors Association (PSPA) is a seafood trade association of 74 years standing, representing the processors segment and its members account for about 85% of the processed seafood produced in the Pacific Northwest and Alaska. Member companies account for annual gross sales in the neighborhood of one billion dollars.

First, we would like to thank you, Senator Boren, and the Committee for addressing this problem in a timely fashion. As seafood processors, we spend millions of dollars annually for fuel to operate fishing vessels, floating processors and tenders. Naturally, we have traditionally been exempt from paying the 15 cents per gallon federal diesel fuel tax since our operations fall into the "off-road" category. We were very alarmed when we learned of the change which had been made in the collection system as part of the 1987 Omnibus Reconciliation Act. Our industry is a major user of diesel fuel, with some of the larger vessels consuming up to 6,000 gallons per day. At this rate, the tax liability of our member companies becomes a significant part of their overall financial operating picture. Also, since fuel consumption accounts for a large percentage of the fixed costs of these firms, this additional tax presents very real cash flow problems. For the most part, the members of PSPA are not large companies. Virtually all have sales under $250 million annually. The lost use of capital, and the considerable added paperwork caused by this change are, therefore, obstacles we can ill afford at a time when we are striving to compete in the world market.

As an aside, we should also mention that this new system will be an even bigger burden on the tens of thousands of individual commercial fishing vessels around the nation. Many of their vessels are operated by single owner/operators and are small businesses in the most classic sense of the term. The fact is that, in all likelihood, neither the American business community nor the Internal Revenue Service are prepared for the paperwork onslaught posed by this new tax collection system.

Finally, we would like to make a point which differentiates our industry from most other "exempt" groups. It is an obvious but significant fact that our operations not only fall into the "off-road" category, they do not even take place on land. While there may be an argument over what percentage of time a farmer uses his truck on the highways versus on the farm, there can be no doubt that our vessels are permanent off-road users of diesel fuel. Additionally, most of our member companies have extensive operations in the North Pacific off the coast of Alaska. Many of the ports where we buy our fuel are only accessible by boat or airplane and quite often, the entire "highway" system consists of a few miles of dirt road.

We hope that the Committee will take our comments into account as the review of this situation continues. It is very important to our industry that we be returned as quickly as possible to the status of being truly exempt from this financial and paperwork burden.

Sincerely,

Barry D. Collier

Barry D. Collier
President

cc: Senate Finance Committee
Senator Brock Adams
Senator Daniel J. Evans
Senator Mark O. Hatfield
Senator Frank H. Murkowski
Senator Bob Packwood
Senator Ted Stevens

TESTIMONY BY

HARRY A. SPANNAUS

BEFORE THE COMMITTEE ON FINANCE
SUBCOMMITTEE ON ENERGY AND AGRRICULTURE TAXATION
MARCH 18, 1988

A B S T R A C T

TESTIMONY IS OFFERED BY THE PERMIAN BASIN PETROLEUM ASSOCIATION, A PETROLEUM INDUSTRY TRADE ASSOCIATION LOCATED IN WEST TEXAS AND SOUTHEASTERN NEW MEXICO AND OTHER INDUSTRY RELATED ASSOCIATIONS NAMELY, THE TEXAS INDEPENDENT PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE KANSAS INDEPENDENT OIL AND GAS ASSOCIATION, THE NORTH TEXAS OIL AND GAS ASSOCIATION, THE WEST CENTRAL TEXAS OIL AND GAS ASSOCIATION, THE EAST TEXAS PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE PANHANDLE PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE COASTAL OIL AND GAS ASSOCIATION AND THE INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO.

WE BELIEVE THAT THE NEW TAXING REQUIREMENTS ON OFF-ROAD DIESEL FUEL AS REQUIRED BY THE OMNIBUS BUDGET RECONCILIATION ACT OF 1987, IS UNJUST AND UNFAIR TO ALL LEGITIMENT USERS OF OFF-ROAD FUELS. IT POSES AN ADDED CASH FLOW BURDEN ON DIESEL FUEL USERS, IT CREATES ADDITIONAL ADMINISTRATIVE EXPENSES FOR BOTH THE USER AND THE IRS IN COMPLIANCE AND VALIDATION AND IT IS A TAX ONLY TO HELP CLOSE ALLEDGED WIDE-SPREAD EVASION OF DIESEL FUEL TAX PAYMENTS TO THE FEDERAL GOVERNMENT WHICH HAS LITTLE IF ANY RELATIONSHIP WITH THE PETROLEUM INDUSTRY OPERATORS OF DIESEL EQUIPMENT.

THE NATION'S DOMESTIC PETROLEUM INDUSTRY IS ATTEMPTING AN ECONOMIC RECOVERY FROM SEVERELY DEPRESSED TIMES. THE FEDERAL GOVERNMENT SHOULD ENHANCE THIS RECOVERY THROUGH FAIR AND JUST LEGISLATION. WE BELIEVE THAT THE NEW TAX REQUIREMENTS ON OFF-ROAD DIESEL FUEL IS CONTRARY TO THIS PHILOSOPHY AND THAT THE LAWS ENACTMENT WILL BE A FURTHER BLOW TO AN INDUSTRY THAT IS ALREADY ON ITS KNEES AND STRUGGLING FOR RECOVERY.

THANK YOU FOR THE OPPORTUNITY TO SUBMIT WRITTEN TESTIMONY. MY NAME IS HARRY SPANNAUS AND I AM EMPLOYED BY THE PERMIAN BASIN PETROLEUM ASSOCIATION AS ITS EXECUTIVE VICE PRESIDENT WITH HEADQUARTERS IN MIDLAND, TEXAS.

THE PERMIAN BASIN PETROLEUM ASSOCIATION HAS OVER 1,300 MEMBERS, COMPOSED OF BOTH MAJOR OIL COMPANIES AND SMALL INDEPENDENT OIL AND GAS PRODUCERS AND RELATED SERVICE AND SUPPLY INDUSTRY MEMBERS, SUCH AS DRILLING CONTRACTORS. THE PERMIAN BASIN IS THE LARGEST SINGLE CRUDE OIL AND NATURAL GAS PRODUCING REGION IN THE LOWER 48 STATES BOTH IN SIZE AND IN PRODUCTION. IT ENCOMPASSES 54 COUNTIES IN WEST TEXAS AND 4 COUNTIES IN NEW MEXICO COVERING OVER 100,000 SQUARE MILES AND IT PRODUCES APPROXIMATELY 23 PERCENT OF THE NATION'S DOMESTIC CRUDE OIL AND 15 PERCENT OF ITS NATURAL GAS.

I AM ALSO TESTIFYING ON BEHALF OF THE TEXAS INDEPENDENT PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE KANSAS INDEPENDENT OIL AND GAS ASSOCIATION, THE NORTH TEXAS OIL AND GAS ASSOCIATION, THE INDEPENDENT PETROLEUM ASSOCIATION OF NEW MEXICO, THE WEST CENTRAL TEXAS OIL AND GAS ASSOCIATION, THE EAST TEXAS PRODUCERS AND ROYALTY OWNERS ASSOCIATION, THE PANHANDLE PRODUCERS AND ROYALTY OWNERS ASSOCIATION, AND THE COASTAL OIL AND GAS ASSOCIATION, WHOSE COMBINED MEMBERSHIP IS IN EXCESSIVE OF 10 THOUSAND MEMBERS WITH COMPOSITIONS LIKE THAT OF MY ASSOCIATION.

WE COMMEND THIS COMMITTEE FOR CONDUCTING THIS HEARING TODAY. WE BELIEVE IT IS IMPORTANT IN THIS TIME OF DOMESTIC PETROLEUM INDUSTRY DEPRESSION TO TAKE WHATEVER MEASURES THAT ARE REASONABLE AND NECESSARY TO PROVIDE FAIR AND JUST TAXATION TREATMENT TO AN INDUSTRY THAT IS ALREADY ON ITS KNEES AND FIGHTING FOR RECOVERY.

THE NEW LAW TO COLLECT "UP-FRONT TAXES" FOR PREVIOUSLY EXEMPT OFF-ROAD DIESEL FUEL USE IS ANOTHER AMONG MANY RULES AND PROPOSALS WHICH WILL HAVE A NEGATIVE IMPACT ON OUR INDUSTRY---ESPECIALLY THE DRILLING CONTRACTORS AND VARIOUS WELL SERVICE COMPANIES WHO CONSUME LARGE QUANTITIES OF DIESEL FUEL FOR DRILLING AND DOWN HOLE SERVICE OPERATIONS.

BEFORE I GET INTO SPECIFIC EFFECTS THAT THE NEW TAX RULING WILL HAVE ON MUCH OF THE INDUSTRY, I WANT TO PROVIDE YOU A BRIEF SUMMARY ON THE HEALTH OF THE DOMESTIC PETROLEUM INDUSTRY; MORE ESPECIALLY THAT OF THE PERMIAN BASIN OF WHICH ITS PRIMARY INDUSTRIAL BASE IS THAT OF OIL AND GAS, BUT ALSO, THE DOMESTIC INDUSTRY THROUGHOUT MAJOR PRODUCING STATES IN THE NATION, AS WE ALL FACE THE SIMILAR DIFFICULTIES.

THE CONTRACT DRILLING AND WELL SERVICING INDUSTRY IS IN VERY POOR SHAPE. THE WESTERN COMPANY, ONE OF OUR LARGEST WELL SERVICING COMPANIES, JUST RECENTLY FILED FOR CHAPTER ELEVEN BANKRUPTCY. SEVERAL OF OUR DRILLING CONTRACTORS SUCH AS MGF AND LOFFLAND BROTHERS, HAVE BEEN UNDER CHAPTER ELEVEN PROCEDURES AND CONSTRAINTS FOR MANY MONTHS AND TODAY, ARE STILL STRUGGLING FOR SURVIVAL. WITHIN THE PERMIAN BASIN, NEARLY 40 PERCENT OF OUR FIRMS ENGAGED IN DRILLING AND WELL SERVICES JUST A FEW YEARS AGO, ARE NOW OUT OF BUSINESS. THEIR PLIGHT IS SHOWN MOST DRAMATICALLY BY THE BASIN'S DAILY OPERATING RIG COUNT WHICH WENT FROM A HIGH OF 529 IN JANUARY 1982 TO A LOW OF 74 IN SEPTEMBER 1986. IT IS NOW FAIRLY CONSTANT AT 145 OPERATING RIGS PER DAY.

IN MIDLAND, OUR SECOND LARGEST EMPLOYER OF EMPLOYEES CONTINUES TO BE THE FDIC WHICH QUARTERLY, HOLDS THE NATION'S LARGEST GARAGE SALE, AND WHERE AUCTION SALES REVENUE COME FROM GOODS AND EQUIPMENT OBTAINED FROM FORECLOSURES AND FAILURES OF PETROLEUM INDUSTRY BUSINESSES.

BANK FAILURES HAVE HIT AN ALL TIME HIGH IN TEXAS AND MOST PRODUCING STATES, AS HAVE BUSINESS FAILURES. IN SHORT, WE NEED SOUND LEGISLATION TO ENHANCE OUR INDUSTRY; NOT ADDITIONAL TAX BURDENS WHICH WILL INCREASE OUT GOING CASH FLOW WITHOUT REVENUE GENERATION IN RETURN AND ADD EXTRA OPERATIONAL COSTS FOR GOVERNMENTAL COMPLIANCE PAPERWORK.

WE BELIEVE THE COMMITTEE WOULD LIKE SOME 1987 STATISTICS THAT IT COULD WORK WITH SOME REAL TIME FACTUAL DATA WHICH IS USED IN FORECASTING THE ADVERSE EFFECTS OF THE NEW PRE TAX REQUIREMENTS ON OFF-ROAD DIESEL FUEL PURCHASES.

WE HAVE OBTAINED OUR DATA FROM TWO SMALL INDEPENDENT DRILLING CONTRACTORS, NAMELY GENE SLEDGE DRILLING AND PETERSON DRILLING OF MIDLAND, TEXAS AND TWO OF OUR LARGEST SERVICE COMPANIES, THE WESTERN COMPANY, WHICH RECENTLY FILED CHAPTER ELEVEN FOR REORGANIZATION AND HALLIBURTON SERVICES, WHO FOR THE FIRST TIME IN SEVERAL YEARS, REFLECTED A 1987 PROFIT IN SALES AND SERVICES NATION WIDE.

I REQUEST THE COMMITTEE REFER TO EXHIBIT "A" OF THIS TESTIMONY.

AS PER EXHIBIT "A" BOTH DRILLING COMPANIES DESCRIBED ARE RELATIVELY SMALL, HAVING ONLY FOUR TO FIVE RIGS IN INVENTORY WITH A UTILIZATION RATE OF APPROXIMATELY 75% TO 80% OF TOTAL CAPACITY. AS YOU WILL NOTE, EACH DRILLING COMPANY CONSUMED IN EXCESS OF 650,000 THOUSAND GALLONS OF DIESEL FUEL WITH AN AVERAGE RIG DAILY CONSUMPTION RATE OF OVER 500 GALLONS. CONSIDERING ACTUAL 1987 DATA, IF AN EXCISE TAX OF 15.1 CENTS PER GALLON WAS LEVIED ON GENE SLEDGE DRILLING FOR 1987, THE COMPANY'S TOTAL ADDITIONAL CASH-FLOW OUTLAY WOULD HAVE BEEN $107,000 OR $21,400 PER RIG ANNUALLY. IF YOU ASSUME THAT EACH GENE SLEDGE RIG WAS OPERATING FULL TIME, A SITUATION WE CERTAINLY HOPE TO RECAPTURE, THE COMPANY'S ADDITIONAL CASH OUTLAY DUE TO THE IMPOSITION OF THE EXCISE TAX ON DIESEL FUEL WOULD BE APPROXIMATELY $142,000 PER YEAR.

IN THE CASE OF OUR SERVICE COMPANIES, EXHIBIT "A" DEPICTS FIGURES ON A NATIONAL BASIS.

IT IS UNDERSTANDABLE BY THESE EXHIBITS THAT THE ADDITIONAL CASH FLOW BURDEN COULD BE DEVASTATING, ESPECIALLY TO THOSE SMALL INDEPENDENTS OR COMPANIES FACED WITH CHAPTER 11 PROCEEDINGS OR WHO HAVE OPERATED NEAR OR IN THE RED FOR 1987. FROM ALL KNOWN ESTIMATES FROM ECONOMISTS AND OTHER EXPERTS SUCH AS THE AMERICAN PETROLEUM INSTITUTE, PETROLEUM INFORMATION AND WORLD OIL AND THE OIL AND GAS JOURNAL MAGAZINES, THE DRILLING OUT LOOK AND WELL SERVICING PROJECTIONS FOR 1988 WILL BE MUCH LIKE THAT OF 1987 AND THE INDUSTRY WILL CONTINUE TO STRUGGLE FOR PROFITS. THE ADDITION OF THE EXCISE TAX ON EXEMPT FUELS AND THE CORRESPONDING COSTS FOR COMPLIANCE MAY ONLY HASTEN THE INEVITABLE--THAT OF FURTHER BUSINESS CRISIS OR TOTAL FAILURE.

THE WESTERN COMPANY IS CURRENTLY OPERATING UNDER BANKRUPTCY REORGANIZATION PROCEDURES AND NOT ONLY HAS NOT PROGRAMMED OR BUDGETED FOR THE ADDITIONAL ANNUAL CASH FLOW OF OVER 340 THOUSAND DOLLARS TO MEET EXCISE TAX REQUIREMENTS, BUT CAN ILL AFFORD THE ADDED EXPENSE BURDEN WHEN THEIR REORGANIZATIONAL PROGRAM AS OVERSEEN BY THE COURTS AND IS ONE OF AUSTERE CUTS AND REDUCTIONS IN SUPPORT OF ITS RECOVERY EFFORTS.

HALLIBURTON SERVICES, A DIVISION OF THE HUGE HALLIBURTON COMPANIES COMPLEX, IS MUCH MORE - CAPABLE OF ABSORBING THE INCREASED CASH FLOW REQUIREMENT WITHIN ITS ORGANIZATIONAL STRUCTURE, HOWEVER, IT WAS ONLY UNTIL RECENTLY THAT IT SHOWED AN ANNUAL PROFIT AND AN ADDITIONAL LIABILITY OF OVER 1 MILLION DOLLARS AND THE BURDEN OF ADDED ADMINISTRATIVE COSTS WOULD BE A FURTHER DETRIMENT TO ITS CONTINUED RECOVERY EFFORTS.

THE SMALL INDEPENDENT DRILLING COMPANIES AND OTHERS WHO ARE IN FINANCIAL DIFFICULTIES ARE NOT SURE HOW THEY ARE TO MEET THE NEW TAXING OBLIGATIONS.

REGLARDLESS OF THEIR ABILITY TO RECOVER SUCH TAXES BY FILING FOR REFUNDS FOLLOWING THE YEARS END, THE MONEY HAS NOT BEEN BUDGETED NOR IS THERE A SUFFICIENT RESERVE FUND AVAILABLE TO COVER THE ADDED LIABILITY. TO BORROW THE MONEY FROM A BANKING INSTITUTION, WHICH WOULD BE NEXT TO IMPOSSIBLE FOR MANY, WOULD BE ADDING AN ADDITIONAL CASH FLOW LIABILITY IN INTEREST AND WOULD ONLY DEEPEN THE WOUND ABOUT TO BE INFLICTED. THE REMAINING WAY IS TO CHARGE BACK TO THE CUSTOMER TO RECOVER THE ADDITIONAL COSTS---A PROCEDURE TOTALLY COUNTER PRODUCTIVE AS IT WOULD DESTROY THE SMALL INDEPENDENTS ABILITY TO COMPETE IN A HIGHLY COMPETITIVE MARKET PLACE.

WHILE OFF SHORE DRILLING OPERATIONS ARE FAR DISTANT FROM THE PERMIAN BASIN, THE SAME PROBLEM IS SHARED. ACCORDING TO THE INTERNATIONAL ASSOCIATION OF DRILLING CONTRACTORS, A DRILLING CONTRACTOR HAVING A FLEET OF 20 OFF SHORE DRILLING RIGS WOULD USE APPROXIMATELY 500 THOUSAND GALLONS OF DIESEL FUEL PER MONTH WITH AN ADDITIONAL TAX COST OF OVER $900 THOUSAND PER YEAR.

IN SUMMARY

WE BELIEVE THAT A TAX LEVIED ON THE TAX EXEMPT COMMODITIES SUCH AS DIESEL FUEL, FOR THE IDENTIFIED PURPOSE OF STOPPING THE WIDE-SPREAD EVASION OF DIESEL FUEL TAX PAYMENTS TO THE FEDERAL GOVERNMENT IS UNFAIR, UNJUST AND A DEPRESSANT TO BUSINESS ENHANCEMENT. IT IS AN ACTION WHICH PLACES AN UNDUE BURDEN ON THE MAJORITY TO AID THE IRS IN THE INTERNAL DIFFICULTIES OF THEIR DETECTION AND COLLECTION PROCESS. WHILE WE CANNOT SAY THAT SUCH

EVASIONS DO NOT OCCUR IN THE OIL PATCH, IT IS HIGHLY UNLIKELY THAT DIESEL FUEL USED TO OPERATE WELL SITE EQUIPMENT IS BEING USED FOR ON-ROAD PURPOSES, JUST AS IT IS ALSO UNLIKELY THAT DIESEL FUEL OR HEATING OIL USED FOR HOME HEATING IS ALSO BEING USED FOR ON-ROAD MOTORIZED VEHICLES. THERE ARE NUMEROUS SAFE GUARDS TO PREVENT SUCH EVASIONS, FULLY QUALIFYING PETROLEUM INDUSTRY MOTORIZED OFF-ROAD EQUIPMENT IN A CATEGORY WHICH MOST LIKELY, WILL NOT UTILIZE OFF-ROAD DIESEL FUEL FOR ON-ROAD PURPOSES.

LASTLY, WE BELIEVE THAT A PERMANENT FIX TO THE NEW TAX WOULD BE AN OUTRIGHT REPEAL OF THE COLLECTION POINT FOR FEDERAL EXCISE TAXES ON DIESEL FUEL AS REQUIRED BY THE OMNIBUS BUDGET RECONCILIATION ACT OF 1987. KNOWING OF THE DIFFICULTIES OF SUCH A REPEAL, THE NEXT BEST ALTERNATE WOULD BE TO PROVIDE AN AMENDMENT TO THE BILL SUCH AS H.R. 3865 OR S. 2118 PROPOSES, WHICH WOULD PERMIT TAX FREE SALES OF DIESEL FUEL FOR OFF-ROAD USES OR INFLUENCE THE DEPARTMENT OF THE TREASURY TO EXEMPT THE PETROLEUM INDUSTRY FROM SUCH TAXES AS CURRENTLY EXISTS AND AS WHAT IS THOUGHT TO BE A GRANTED AUTHORITY BY THE CONGRESS.

EXHIBIT "A"

1987 CLASSIFICATION	PETERSON DRILLING	SLEDGE DRILLING
Number of Drilling Rigs	4	5
Number of Drilling Contracts	65	37
Active Drilling Days (All rigs)	1143	1397
Rig Utilization Rate	80%	75%
Diesel Used (Off-Road)	655,321 Gallons	710,546 Gallons
Average Diesel Daily Consumption	573 Gallons	509 Gallons
Diesel Fuel Costs (Off-Road)	$412,852	$585,259
Added Cash Outlay for Excise Taxes	$ 98,953	$107,292

SERVICE COMPANIES

1987 CLASSIFICATION	THE WESTERN COMPANY	HALLIBURTON SERVICES
Number of Diesel Units	726	UNK
Diesel Used (Off-Road)	2,259,290 Gallons	7,500,000 Gallons
Diesel Costs (Off-Road)	$1,581,503	$5,250,000
Added Cash Outlay for Excise Tax	$ 341,153	$1,132,500

The Texas Shrimp Association
First in Fisheries
403 Vaughn Building Austin, Texas 78701
Tel. (512) 476-8446, 476-8447

March 17, 1988

The Honorable Lloyd Bentsen
Chairman
Committee on Finance
205 Dirksen Senate Office Building
Washington, D.C. 20510

RE: the Diesel Fuel Collection Bill

Dear Mr. Chairman:

We are writing you because of our concern about the diesel fuel tax exemption which was changed by the Reconciliation Act of 1988. We believe that requiring fishing vessel operators to apply for a tax refund imposes a significant paperwork burden on these small businessmen. The refund process itself is an additional administrative nightmare for both the applicant and the Federal Government.

As you know, many of our members operate on a narrow margin. They cannot afford for the Federal Government to be using their money and drawing interest upon it. These operators need that money for payment of their vessel mortgages, insurance premiums, vessel and gear repairs and replacement, as well as basic living expenses.

In the shrimp industry, fuel is the major cost of operating the vessel. It accounts for approximately 25 to 33% of operating expenses. An average Gulf shrimp vessel -- 55 to 80 feet long -- uses approximately 50,000 gallons of fuel in a year. In 1987, the average price of diesel fuel to the vessel was $0.62 per gallon. Approximately, $7,550 would be paid as an excise tax if the new law is enacted in April. We do not believe it is equitable to tie up a fisherman's $7,550 when he does not owe that money to the Government.

We respectfully request your assistance in ensuring that the Committee on Finance considers this critical issue when they address technical corrections to the tax bill.

Most sincerely,

Kristin L. Vehrs
Washington Representative

Branch Office: 1110 Vermont Ave. N.W., Suite 1180, Washington, D.C. 20005
Tel. (202) 293-5513

The Texas Shrimp Association
403 Vaughn Building Austin, Texas 78701
Tel. (512) 476-8446, 476-8447
First in Fisheries

21 March 1988

The Honorable Lloyd Bentsen
Chairman
Committee on Finance
205 Dirksen Senate Office Building
Washington, D.C. 20510

Dear Mr. Chairman:

We ask that this letter be made a part of the 16 March hearing record on the diesel fuel tax exemption. We further request that our letter of 17 March to you on this subject be incorporated into our testimony. A copy of that letter is attached.

In discussions with Committee staff, we understand that one of the key concerns regarding the diesel fuel tax exemption change is misuse by individuals not eligible for the exemption. That is one of the issues we wish to address in this letter. The other issues are the various solutions being offered by Committee members.

In the Texas shrimp industry, diesel fuel for use by the fishing industry is generally purchased by a retail-level fuel dock operation from a wholesaler. Typically, that fuel is purchased by the truck load. According to state law, the retail purchaser must have a bonded supplier's permit if the purchaser owns a diesel powered vehicle or if his operation includes other than off-highway users exempt from the diesel fuel tax.

A bonded supplier must account for the amount of fuel sold to highway users and the amount sold to off-highway users. Copies of the fuel receipts from each different user must be sent to the state on a monthly basis. Tax can then be paid on the non-exempt users.

A diesel fuel retailer selling fuel to fishing vessels would not be very likely to sell diesel fuel to other users or use the fuel himself for other purposes. The reason is that there is no physical way to service users other than commercial fishing vessels because of the dock locations, fuel pumps, hoses and nozzles.

Almost all ports located along the Texas coast are separated into two segments: the fishing port and the recreational marinas. Individual fishing vessels purchase fuel either from one of the local fuel docks or perhaps belong to a cooperative. The majority of vessels purchase fuel from a fuel dock

Diesel fuel is pumped into the fuel tanks of a fishing vessel with high volume pumps. The nozzles from these pumps will not fit into a typical fuel tank of a car or a truck. They are of a much larger scale and designed to force thousands of gallons of fuel into tanks in a short period of time. Most fishing operations do not have a fleet of trucks but probably would operate vans or 2-ton gasoline trucks.

In conclusion, we do not believe that either at the retail level or the vessel owner level that the fishing industry appreciably misuses tax exempt diesel fuel.

We will next discuss several options we have heard for solving the up front exemption for tax exempt users. "Allowing all off-road users who purchase from wholesale distributors to purchase tax-free" will aid very few individuals in the fishing industry. There are very few individuals who purchase directly from a wholesaler.

Expanding the permit tax-free sales "on the same basis to exempt users who are not required to make quarterly estimated income tax payments and who are not subject to income tax withholding" will not help fishermen. Most fishermen do not file quarterly estimated taxes but file on a yearly basis on 15 March. However, most vessel owners have incorporated their vessels to avoid personal liabilities and fuel expenses will be applied against the corporation.

Furthermore, most boats operate on a share of the catch basis. Under this arrangement, the crew is paid a salary but a share of the proceeds of the catch and must share expenses with the vessel owner; including diesel fuel in many cases. It would be virtually impossible to determine what share of the diesel fuel refund a crew member should receive; in particular since crew members frequently change vessels.

We respectfully request that the case-by-case exemption of certain non-highway diesel fuel users be expanded to include the marine industry -- specifically commercial vessels in the domestic waterways industry and fishing vessels. Fuel for marine use is distributed through a system which guarantees that all fuel purchased for such use will not be diverted to highway use.

Thank you for the opportunity to submit these additional comments regarding the diesel fuel tax exemption. The Texas Shrimp Association looks forward to working with you and your staff on this most important issue.

Sincerely,

Kristin L. Vehrs
Washington Representative

CC: The Honorable Bill Bradley
The Honorable John H. Chafee
The Honorable William S. Cohen
The Honorable George J. Mitchell
The Honorable Bob Packwood